**COMMONWEALTH OF KENTUCKY**

**BEFORE THE PUBLIC SERVICE COMMISSION**

**IN THE MATTER OF:**

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| **ELECTRONIC APPLICATION OF** | ) | |
| **KENTUCKY-AMERICAN WATER** | ) | |
| **COMPANY FOR AN ADJUSTMENT OF** | ) | CASE NO. |
| **RATES, APPROVAL OF SYSTEM** | ) | 2026-00094 |
| **IMPROVEMENT PROGRAM, AND** | ) | |
| **TARIFF CHANGES** | ) | |

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# POST-HEARING BRIEF OF KENTUCKY-AMERICAN WATER COMPANY

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**Filed: November 9, 2026**

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## I. STATEMENT OF THE CASE

On April 15, 2026, Kentucky-American Water Company ("KAWC" or "Company") filed a Notice with the Kentucky Public Service Commission ("Public Service Commission" or "Commission") in conformity with 807 KAR 5:001, Section 16(2), expressing its intention to file an application for an increase in rates no earlier than 30 days from the date of the Notice. The Notice specifically provided that the Application for an increase in rates would be supported by a fully forecasted test period as authorized by KRS 278.192.

In keeping with prior practice, simultaneously with the delivery of its Notice to seek an increase in rates, KAWC submitted a Notice of Election of Use of Electronic Filing Procedures. By letter dated April 15, 2026, the Commission's Executive Director assigned a case number to the proceeding. KAWC filed its Application and supporting materials, including the direct testimonies of: Ann E. Bulkley; Robert Burton; William A. Lewis; John Magner; Robert V. Mustich; Jeffrey Newcomb; Robert Prendergast; Charles B. Rea; Linda Schlessman; John M. Watkins; and Joseph Weiss on May 15, 2026.

In its Application filed with the Commission, KAWC sought the Commission's approval of an increase in its annual revenues of $17,684,459 by rates to become effective on or after December 14, 2026 (including a rate suspension period) and approval of proposed tariff revisions.[1]

The adjudication of this matter has proceeded with three intervenors: the Attorney General ("AG"), Lexington-Fayette Urban County Government ("LFUCG"), and Georgetown Municipal Water and Sewer Service ("GMWSS") (collectively, "Intervenors"). On May 18, 2026, the AG filed a motion to intervene. The Commission granted the motion on May 20, 2026, and ordered the AG to comply with the service and electronic filing requirements. On May 21, 2026, LFUCG

[1] Application, Exhibit 37A, Page 2 of 2 (May 15, 2026).

moved for full intervention, agreed to electronic transmission of all notices and messages in this proceeding, and certified its ability to receive electronic transmissions. The Commission granted LFUCG's motion to intervene on June 4, 2026. On June 2, 2026, GMWSS filed a motion to intervene. The Commission granted the motion on June 17, 2026, and ordered GMWSS to comply with the service and electronic filing requirements.

By letter dated May 21, 2026, the Commission's Executive Director informed all parties of record that the Application met the minimum filing requirements and was accepted for filing as of May 15, 2026.

On May 27, 2026, the Commission entered an Order suspending the proposed rates for a period of six months and established a Procedural Schedule providing for two rounds of data requests to KAWC, the filing of intervenors' testimony, one round of data requests to the intervenors, the filing of rebuttal testimony by the Company's witnesses, and an evidentiary hearing in this matter to begin on October 13, 2026.

On August 7, 2026, the Intervenors co-presented the testimonies of Aaron L. Rothschild and John Defever. GMWSS separately presented the testimony of Chase Azevedo.

On September 16, 2026, KAWC filed its Base Period Update in which it revised its revenue requirement downward from $180,168,709 to $180,153,194 and revised its revenue deficiency and requested annual increase downward from $17,684,459 to $17,669,653.[2] Additionally, rebuttal testimony was presented from Ann E. Bulkley; William A. Lewis; Jeffrey Newcomb; Robert Prendergast; Charles B. Rea; and John M. Watkins.

During the pendency of this proceeding, KAWC closed its acquisitions of the water systems of the Water Service Corporation of Kentucky, as well as Black Mountain Utility District

[2] Base Period Update Filing Exhibit 37A, Page 2 of 2 (Sep. 16, 2026).

("Black Mountain"). In the Water Service Corporation of Kentucky acquisition, the Company filed its joint application for Commission approval of the acquisition on May 30, 2025, and received Commission approval on September 9, 2025.[3] In the Black Mountain acquisition, the Company and Black Mountain filed their Joint Application for Commission approval of their Asset Purchase Agreement ("APA") on April 20, 2026, and received Commission approval on July 10, 2026.[4] KAWC closed its acquisition of Water Service Corporation of Kentucky on June 1, 2026, and its acquisition of Black Mountain on October 9, 2026.[5]

A hearing on the merits of the requests presented in KAWC's Application was held at the Commission on October 13 and 14, 2026. The following witnesses for KAWC were presented and made subject to cross-examination: Ann E. Bulkley; Robert Burton; William A. Lewis; John Magner; Robert V. Mustich; Jeffrey Newcomb; Robert Prendergast; Charles B. Rea; Linda Schlessman; John M. Watkins; and Joseph Weiss.

Pursuant to the Commission's Order dated October 20, 2026, a schedule for post-hearing discovery and submission of briefs was established. Commission Staff and the AG served requests for information in accordance with that schedule and the Company timely filed its responses to these requests. KAWC likewise issued requests for information to the Intervenors. LFUCG moved to strike KAWC's post-hearing request No. 3, in which KAWC sought confirmation of LFUCG sewer rate increases. KAWC responded to LFUCG's Motion to Strike on November 6, 2026.

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[3] *Verified Application of American Water Works Company, Kentucky-American Water Company, Nexus Regulated Utilities, LLC, and Water Service Corporation of Kentucky for Approval of the Transfer of Control of Water Service Corporation of Kentucky*, Case No. 2025-00171, Application (Ky. PSC May 30, 2025); *Id.*, Order (Ky. PSC Sep. 9, 2025).

[4] *Electronic Joint Application of Black Mountain Utility District and Kentucky American Water Company for the Transfer of Control and Assets,* Case No. 2026-00097, Application (Ky. PSC Apr. 20, 2026); *Id.*, Order (Ky. PSC July 10, 2026).

[5] Case No. 2025-00171, Ordering Paragraph 4 Report (Ky. PSC June 8, 2026); Case No. 2026-00097, Kentucky-American Water Company's Closing Report (Ky. PSC Oct. 9, 2026).

## II. SYSTEM IMPROVEMENT PROGRAM

In Case No. 2018-00358, the Commission approved the Company's Qualified Infrastructure Program ("QIP") to promote smaller, more gradual rate increases and to facilitate capital recovery while reducing the frequency of rate cases.[6] In Case No. 2025-00122, the Commission ended the QIP, finding that KAWC failed to consistently utilize the rider and that the QIP was no longer achieving its intended purpose of reducing rate case frequency.[7]

Despite the QIP's termination, the need to replace aging water infrastructure and upgrade water treatment systems persists.[8] These ongoing capital investments are the impetus for this rate case. Indeed, both internal and external analyses demonstrate the Company will need to continue investing in its system for the foreseeable future.[9]

### (A) Ongoing System Investments are Required to Maintain Adequate Service

KAWC has operated in Kentucky for approximately 140 years and maintains more than $1.1 billion of water infrastructure[10] constructed at different times, from different materials, and with different standards.[11] To manage the pressure of aging assets, regulatory compliance, system demands, safety, and service quality, KAWC deploys a robust capital planning program. Key associated processes include comprehensive planning studies, pipeline prioritization modeling, targeted studies, and risk and resiliency assessments.[12] Teams also work to control costs through shared restoration, value engineering, price negotiations, competitive bidding, project scoping, internal design development, and a proactive approach to asset replacement.[13] Within this

[6] Case No. 2025-00122, Order at 41 and 44 (December 16, 2025).
[7] Case No. 2025-00122, Order at 43-45 (December 16, 2025).
[8] *See* Direct Testimony of John Magner at 30-31 (May 15, 2026).
[9] *Id.* at 31-32.
[10] Application at Exhibit 37 B-1; Base Period Update Filing Exhibit 37 B-1.
[11] Magner Direct at 30.
[12] *Id*. at 3
[13] *Id*. at 12-15

framework, KAWC's near-term capital plans show needs in excess of $100 million annually.[14] This includes more than $65 million per year in normal recurring projects, including pipe replacement, with external estimates suggesting the Company needs to replace 0.85 – 1.0% of its water mains per year.[15] Additionally, plans reflect $20 million to $40 million of annual spend on investment projects, especially treatment facilities, tanks, and booster stations.[16]

The Company's system is not unique in requiring significant investment. The EPA's 2023 analysis of Kentucky water systems estimated that Kentucky's drinking water infrastructure requires at least $7.8 billion of investment over the next 20 years.[17] What separates the Company from other Kentucky water utilities is its willingness to proactively make these repairs and its holistic replacement analysis that includes not only the age of components, but also the likelihood of failure and the cost impact of the ongoing investments.[18] KAWC's approach to system investments is in the long-term best interest of customers and involves extensive analysis, constant communication with operations staff, and an array of cost-control measures including cost-sharing and thoughtful timing.[19]

**(B) <u>The SIP is Designed to Resolve the Commission's Concerns with the Discontinued QIP Mechanism</u>**

Because a well-designed surcharge mechanism can facilitate efficient capital investment and yield benefits for customers, KAWC took note of the Commission's critiques of the QIP and developed its System Improvement Program ("SIP") with four responsive improvements:

- Continuous rider operation with rate case identification of SIP projects;[20]

[14] Application at Exhibit 11.
[15] Magner Direct at 34.
[16] Application at Exhibit 11.
[17] Magner Direct at 31; Oct. 13, 2026 Hearing, VR (3:29:01 PM – 3:29:42 PM).
[18] Oct. 13, 2026 Hearing VR (3:25:00 PM – 3:27:40 PM).
[19] *Id.*; Magner Direct at 36.
[20] KAWC response to PSC 2-41(a) (June 26, 2026).

- A separate line item on bills[21] that remains after approval of new base rates, unless reset to zero by the Commission;[22]
- A broader asset scope better aligned to capital investment needs to extend the time between rate cases;[23] and
- A GRC Balancing adjustment to support reduced rate case frequency.[24]

**(C) <u>The SIP's Broader Asset Scope and GRC Balancing Adjustment are Crucial to its Efficacy in Reducing Rate Cases</u>**

As Mr. Newcomb addressed in his rebuttal testimony, the primary drivers of rate cases during the years that the QIP was in place were capital investments that the Company could not recover through its QIP.[25] Maintaining the SIP's broader scope of eligible projects, including mains, hydrants, valves, service lines, SCADA equipment, and other necessary infrastructure, will greatly improve the Company's ability to increase the interval between rate cases.[26] Likewise, the GRC Balancing Adjustment can prevent lag on eligible investments not fully captured in rates.[27] Indeed, if current conditions hold, the proposed SIP could forestall the Company's next rate case until 2029.[28]

**(D) <u>Providing the Same ROE for SIP and Non-SIP Investments is Appropriate and Aligns Company Incentives with Customer Benefits</u>**

Ms. Bulkley's research and analysis demonstrate that her recommended ROE is appropriate and reasonable for both KAWC's base rates and the proposed SIP mechanism.[29] As established by Ms. Bulkley, 75 percent of the utilities within her proxy group have comparable

[21] Direct Testimony of Jeffrey Newcomb at 23 (May 15, 2026).
[22] KAWC response to PSC 2-41(a).
[23] Magner Direct at 31-49.
[24] KAWC response to PSC 2-41(a).
[25] Rebuttal Testimony of Jeffrey Newcomb at 3 (Sep. 16, 2026).
[26] Newcomb Direct at 6.
[27] KAWC response to PSC 2-41(a)
[28] Newcomb Direct at 10; Newcomb Rebuttal at 5; October 13, 2026 Hearing VR (2:38:21 PM – 2:38:54 PM).
[29] Bulkley Rebuttal at 67-68.

mechanisms to recover the cost of capital expenditures outside of general rate proceedings.[30] Ms. Bulkley's ROE modeling incorporates the effect of these mechanisms on the proxies' overall ROE.[31] As such, if the ROE is reduced for the proposed SIP mechanism, the Company is mistakenly being treated as less risky than the proxy group, which Ms. Bulkley's detailed analysis clearly refutes.

Mr. Rothschild also argues that the balancing mechanism and other customer protections in the proposed SIP reduce risk for the Company.[32] As discussed by Mr. Newcomb, the SIP's Balancing Adjustment functions primarily as a true-up mechanism and an important form of customer protection, not a reduction of risk for the Company. As Mr. Newcomb points out, KAWC has experienced year-over-year growth in billing determinants.[33] The operation of the Balancing Adjustment reconciles SIP revenues with the actual costs associated with the SIP's in-service investment. To the extent growth in billing determinants produces excess revenue as compared to investment costs, the Balancing Adjustment shields customers from over-recovery rather than providing KAWC with an opportunity to earn additional revenue.[34] The SIP's Balancing Adjustment therefore is a customer protection that should not be characterized simply as a reduction of KAWC's risk because it operates symmetrically between customers and the Company to align recovery with actual qualifying investment and associated costs.

Additionally, as discussed by Mr. Newcomb, reducing the ROE applied to KAWC's proposed SIP is not appropriate, as it could impact KAWC's competitiveness for investment dollars and discourage use of the SIP.[35] The Company could instead file annual GRCs that utilize

[30] *Id.* at 67-68.
[31] *Id.*
[32] Rothschild Direct at 79-80.
[33] *Id.* at 8.
[34] *Id.* at 6-7.
[35] Rebuttal Testimony of Jeffrey Newcomb at 6-9 (Sep. 16, 2026).

a future test period, which would allow recovery at the Commission-authorized ROE for base rates; however, it would not provide the same gradualism, regulatory efficiencies, customer benefits, or reduced rate case frequency that the proposed SIP is designed to achieve.[36] If the purpose of authorizing a new capital rider is to encourage more consistent use than existed with prior models and to discourage rate cases, an ROE reduction would be a step in the wrong direction.

Finally, to the Company's knowledge, the Commission has not previously reduced the ROE applicable to water utility capital mechanisms, including KAWC's former QIP capital mechanism.[37]

For all of the above reasons, if the Commission's intent is to discourage frequent rate cases, promote more consistent use of authorized capital mechanisms, and maintain fair, just, reasonable rates while gradualizing customer bill impacts, a SIP ROE consistent with general rate case ROE will best support those goals.

## (E) The SIP is an Efficient Capital Mechanism that Will Benefit Customers

### *1) Annual SIP filings with multi-year forecasts provide greater transparency for upcoming investments and rate impacts[38]*

The SIP provides project-by-project transparency. As part of the SIP mechanism, the Company will submit annual filings accompanied by a forecast year, maintain a rolling three-year plan, and disclose any shifts in spending.[39] Exhibit JN-1 serves as a foundational filing for the SIP

[36] *Id*. .and Newomb Direct at 7-8
[37] *Id*. at 9.
[38] Newcomb Direct at Exhibit JN-1.
[39] Newcomb Direct at 8 (May 15, 2026).

mechanism, providing the first of these three-year views, including a multi-year forecast for capital expenditures by project along with projected SIP rate impacts.[40]

*2) **The SIP gradualizes customer rate increases***

By providing annual relief for qualifying investments, the SIP mechanism smooths rate increases for customers and prevents rate shock.[41]

*3) **The SIP can reduce regulatory expense for customers***

The narrow scope of the SIP compared to a GRC would minimize regulatory expense for customers while still providing the opportunity for public involvement in and Commission oversight of the Company's investments.[42]

***4) The SIP promotes proactive asset replacement to minimize costly emergency repairs.***

The Company's forward-looking capital investment plan helps it both maintain adequate service *and* control infrastructure costs. As Mr. Magner explained at the hearing, executing system improvements *before* failure occurs allows the Company to control replacement costs.[43] The Company's 2023 analysis of these cost differences estimated that the Company's planned main replacements cost roughly $330 per linear foot, while emergency replacements cost $1,000 per linear foot.[44] In short, the need for capital investments is very real, and the Company's proactive, planned system investments ensure that the Company is able to control costs and avoid the unnecessary expense of emergency repairs.

***5) Improved SIP mechanics resolve Commission QIP concerns, while delivering multiple customer protections, including scope limitations, multiple review***

[40] *Id*. at 18, Exhibit JN-1.
[41] *Id*. at 10.
[42] *Id*. at 9-10.
[43] Oct. 13, 2026 VR (3:30:34 PM – 3:30:51 PM) ("I also note that just because we don't see other utilities investing or raising rates, I don't think that's necessarily the most prudent approach. Because eventually that infrastructure is going to fail, and when you see failures where you haven't made that investment in emergency conditions, it gets much more expensive.").
[44] *See* Magner Direct at 14-15. Indeed, KAWC's response to LFUGC 1-49 provides the cost of emergency replacement $2,124.61 per linear foot and $2,621.39 per linear foot in 2024 and 2025, respectively.

***periods, approval necessary for inclusion of CPCN or acquisition-related investments, and balancing adjustments***

In addition to the improvements identified to address PSC concerns, the SIP also provides meaningful customer protections.[45] The Company will deploy a Balancing Adjustment that reconciles forecasted costs to actual costs, ensuring that customers pay no more and no less than the actual costs of the investments.[46] Both the annual filings and the balancing adjustments will be subject to a 90-day review period.[47]

The SIP's project scope is appropriately limited. The mechanism only includes qualified, non-revenue-producing ("non-growth") plant investments that are incremental to recovery in the most recent water GRC.[48] Additionally, the eligible asset categories are fixed in the SIP tariff and cannot be altered or expanded without Commission approval.[49] The Company must also seek approval to include any investments that require a CPCN or that arise from an acquisition.[50] Finally, the three-year forecasts provide the Commission an opportunity to assess whether the Company's planned investments are consistent with the SIP's scope.[51]

In summary, the proposed SIP will advance the Commission's objective to reduce rate case frequency and regulatory costs, gradualize rate impacts for customers, maintain fair, just, and reasonable rates as KAWC makes necessary system investments, and give the Commission and other stakeholders a view of the Company's planned system investments in advance.

[45] Newcomb Rebuttal at 5.
[46] *Id*. at 6.
[47] Newcomb Direct at 17.
[48] KAWC response to PSC 4-8(a) (Sep. 10, 2026).
[49] Newcomb Rebuttal at 7.
[50] Newcomb Direct at 22.
[51] Newcomb Rebuttal at 7.

The Company has demonstrated that the SIP is calibrated to achieve the goals of an effective infrastructure improvement surcharge, and the Commission should approve the SIP as proposed.

## III. REVENUE REQUIREMENT

KAWC's revenue requirement reflects the cost of providing water service to approximately 150,000 water service connections across its service territory in all or portions of seventeen[52] Kentucky counties.[53] Providing water service is a sprawling endeavor that starts with sourcing more than fifteen billion gallons of surface water from Kentucky lakes and rivers, then treating it to meet or surpass drinking water standards, and finally pumping and distributing it through approximately 2,400 miles of main to reach homes, businesses, schools, and industries throughout KAWC's service territory.[54] Along the way, the Company must work to provide adequate capacity and storage to accommodate peak usage and to help protect communities during fire events.[55] KAWC also provides customer service, monthly billing, 24-hour emergency call handling, and a self-service website.[56] KAWC monitors water quality for a host of contaminants and maintains the distribution system by exercising valves, flushing hydrants, and repairing main breaks at all hours and in all weather conditions.[57] All these efforts support KAWC's provision of safe, clean, reliable water service, sanitation, and fire protection service to customers.[58]

[52] Bell, Bourbon, Clark, Fayette, Franklin, Gallatin, Grant, Harlan, Harrison, Hickman, Jackson, Jessamine, Nicholas, Owen, Rockcastle, Scott, and Woodford Counties.
[53] Direct Testimony of William A. Lewis at 3, 8-9 (May 15, 2026); Direct Testimony of John M. Watkins at 6 (May 15, 2026).
[54] Watkins Direct at 7.
[55] *Id.*
[56] *Id.*
[57] *Id.*
[58] *Id.*

To accomplish this, KAWC incurs costs for which it seeks recovery through the ratemaking process. The Company's costs include a variety of operating expenses, depreciation and amortization, and various local, state, and federal taxes.[59] KAWC must also provide a return—at least equal to the cost of capital—on over $735 million in water infrastructure rate base that supports the Company's provision of service to customers.[60] KAWC's forecasted revenue requirement in this proceeding, equal to the cost of providing service, is approximately $180.15 million for the twelve months ending December 31, 2027.[61]

The difference between the forecasted revenue requirement and KAWC's forecasted revenues at present rates equates to KAWC's revenue deficiency.[62] The Company's revenue deficiency in this proceeding, reflective of the Base Period Update, is calculated to be approximately $17.67 million, which is an approximate 10.87 percent shortfall.[63] The primary driver of the revenue deficiency in this case is the cost of the significant investments KAWC is making into its infrastructure, which make up the largest portion of the Company's total requested increase.[64]

KAWC, through its Application, witness testimony, and responses to data requests, has presented evidence to justify its proposed revenue requirement, which is composed of numerous components. The following revenue requirement components have been directly contested by the AG, LFUCG, and GMWSS: employee-related expenses, including labor, overtime, performance compensation, temporary-help expenses for vacancies, and non-labor costs; the absence of a cash working capital request and accompanying lead-lag study; business development expenses;

[59] *Id.*
[60] *Id.*
[61] Base Period Update Filing Exhibit 37, Schedule A.
[62] Direct Testimony of Robert Burton at 5 (May 15, 2026).
[63] *Id*.
[64] *Id.* at 5-6.

miscellaneous expenses; water losses; rate case expense; sale for resale rates; rate of return; capital structure; single-rate tariff structure; and the terms of KAWC's proposed System Improvement Program.[65] Using Mr. Rothschild's recommendations regarding cost of capital, his own itemized adjustments, and the removal of certain categories of expenses, Mr. Defever recommended an overall revenue decrease of $3.384 million.[66] A review of the evidentiary record demonstrates KAWC's proposals related to each of these contested components are reasonable and should be adopted and that Mr. Defever's recommendations should be rejected.

**(A) Employee-Related Expenses**

Employee-related expenses include direct labor expenses, such as base salary and wages and performance pay, and non-labor expenses such as payroll tax, employee benefits, and group insurance costs. KAWC's forecasted labor expense is based on a projected staffing level of 206 full-time equivalents. The Company explains the reasonableness of these expenses in detail below.

***(1) KAWC's Forecasted Headcount and Labor Expense Are Reasonable and Consistent with Longstanding Commission Precedent.***

The forecasted test period labor expense is based on KAWC's planned staffing level at hourly rates per contract for union employees and wage rates for non-union employees that reflect forecasted pay increases.[67] Because a portion of labor and labor-related costs are capitalized with capital projects and programs, a capitalization percentage is used to assist in calculating net expense.[68] An adjustment is also made to remove costs appropriately charged to wastewater operations.[69] As a result, O&M labor expenses represent costs related to water operations that are charged to expense.[70]

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[65] *See generally* Direct Testimony of John Defever (Aug. 7, 2026). *See also* Section II *infra*.
[66] Defever Direct at 4-5.
[67] Direct Testimony of Robert Prendergast at 6 (May 15, 2026).
[68] *Id.*
[69] *Id*.
[70] *Id.*

KAWC's forecasted labor expense is based on a projected staffing level of 206 full-time equivalents, an increase of 38 employees above the Company's 2025 estimate, 29 of which are directly related to the three closed acquisitions. This staffing level reflects the Company's reasonable estimate of the additional labor necessary to support new water treatment processes, substantial system-wide improvements and construction, approximately 10,000 additional customer connections in newly acquired systems, and continued regionalization.[71] KAWC's proposed headcount additions are entirely a function of the new infrastructure demands across its system, and the Company plans to staff portions of its new systems with existing employees where possible.[72]

For thirty years, KAWC has forecasted its labor expense based on the number of employees that are required to complete the work to continue to provide safe and reliable water service to its many customers throughout its service territory. This operational requirement exists regardless of whether every authorized employee position is filled at a particular point in time. While the timing and duration of vacancies fluctuate, a vacancy does not eliminate the work associated with the position or demonstrate that the position is unnecessary. The work necessary to continue to operate KAWC's system and continue to provide reliable service remains and must still be performed.

During the evidentiary hearing, the Intervenors' witness John Defever acknowledged that vacancies are typical for water utilities[73] and that the Commission has never required a utility to apply a proposed vacancy factor to headcount.[74] With a set amount of work to be accomplished each year, when KAWC has vacant employee roles, the work that would be performed by those vacant positions is either (a) delegated to other KAWC employees, and the Company incurs

[71] Lewis Direct at 39, 42.
[72] *Id.* at 42, 45.
[73] Oct. 14, 2026 Hearing VR (12:41:49 PM – 12:42:23 PM).
[74] Oct. 14, 2026 Hearing VR (12:42:45 PM – 12:43:22 PM).

additional expenses for overtime pay, or (b) contracted to laborers outside of the Company, and the Company incurs additional expenses for contract services. As demonstrated in Mr. Prendergast's Rebuttal Exhibit RP-2R, from 2022 through 2026, the Company spent more than authorized levels for labor, overtime, and contract services.[75]

For ratemaking purposes, the Company has historically forecasted its labor expense based on the salaries and wages owed to the number of employees required to complete KAWC's work, instead of forecasting how much potential overtime or contracted labor expenses may result from an unknown number of vacant employee roles. The Commission has consistently approved this approach in Orders issued in 1996,[76] 2005,[77] 2010,[78] 2019,[79] 2024,[80] and 2025.[81] The Intervenors' argument is not new. In each of those six cases, the AG (and LFUCG in Cases No. 2018-00358, 2023-00191, and 2025-00122) argued that vacant positions should be excluded from forecasted labor expense. The Commission has consistently declined to adopt that position. As the Commission has previously recognized, focusing solely on the reduction in direct labor expense associated with vacancies fails to account for increases in corresponding costs incurred to perform the work, including increased overtime, contractor expense, and temporary labor costs.[82]

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[75] Rebuttal Testimony of Robert Prendergast at Exhibit RP-2R (Sep. 16, 2026).
[76] *Application of Kentucky-American Water Company to Increase its Rates*, Case No. 95-554, Order at 32 (Ky. PSC Sept. 11, 1996).
[77] *Adjustment of the Rates of Kentucky-American Water Company*, Case No. 2004-00103, Order at 44 (Ky. PSC Feb. 28, 2005).
[78] *Application of Kentucky-American Water Company for an Adjustment of Rates Supported by a Fully Forecasted Test Year*, Case No. 2010-00036, Order at 24-25 (Ky. PSC Dec. 14, 2010).
[79] *Electronic Application of Kentucky-American Water Company for an Adjustment of Rates*, Case No. 2018-00358, Order at 37-40 (Ky. PSC June 27, 2019).
[80] *Application of Kentucky-American Water for an Adjustment of Rates, a Certificate of Public Convenience and Necessity for Installation of Advanced Metering Infrastructure, Approval of Regulatory and Accounting Treatments, and Tariff Revisions*, Case No. 2023-00191, Order at 19-20 (Ky. PSC May 3, 2024).
[81] *Application of Kentucky-American Water for an Adjustment of Rates supported by a Fully Forecasted Test Year*, Case No. 2025-00122, Order at 19-20 (Ky. PSC Dec. 16, 2026).
[82] Case No. 2018-00358, Order at 39 (Ky. PSC June 27, 2018). *See also* Case No. 2025-00122, Order at 19-20 (Ky. PSC Dec. 16, 2026) ("the Attorney General/LFUCG's adjustment does not account for an increase in overtime, contractor labor, or temporary employee labor to offset the unfilled positions").

That reasoning remains applicable here. As mentioned above, Mr. Defever acknowledged that vacancies are typical for utilities and that this Commission has not required a utility to apply a vacancy adjustment to headcount. The existence of vacancies does not demonstrate that KAWC's forecasted positions are unnecessary, or that the work underlying those positions will not be performed. The Commission should therefore continue its established treatment and accept KAWC's forecasted staffing level.

***(2) The Intervenors' Vacancy Adjustment is Inconsistent and Overstates the Proposed Reduction***

Mr. Defever proposes a $1,480,953[83] pre-tax adjustment to payroll expense to reflect an average 5.4% vacancy rate for the years 2021 through 2025. Mr. Defever also recommends a *downward* adjustment to both overtime and temporary-help expenses.[84] This methodology reduces the costs associated with vacancies while simultaneously reducing the costs KAWC incurs to perform the work during those vacancies. This ignores the Commission's previous orders approving bilateral adjustments and the Company's increased staffing needs.[85] Additionally, Mr. Defever's recommendation is inconsistent with the relationship between vacancies and other labor resources necessary to perform KAWC's work. If KAWC's forecasted payroll is reduced based on the premise those positions will remain vacant, the analysis must also account for the costs of performing the work associated with those vacancies, including overtime, temporary labor, and contracted services. Again, KAWC demonstrated in Mr. Prendergast's Rebuttal Exhibit RP-2R that from 2022 through 2026the Company has spent more than authorized levels for labor,

[83] Based on his proposal for payroll expense, Mr. Defever also proposes "flow through" reductions for payroll tax ($267,926) and benefits expense ($414,192). Defever Direct at 5. Because his payroll expense proposal should be rejected, his "flow through" proposals should likewise be rejected.
[84] Defever Direct at 10-11, 18-19.
[85] Defever Direct at 18-19; Rebuttal Testimony of William A. Lewis at 3-4 (Sep. 16, 2026).

overtime, and contract services.[86] Therefore, the Company's as-filed position provides the most cost-effective methodology for customers when the Company is faced with vacancies.

The Company's work must be completed with available resources, which consist of full-time employees, overtime, temporary employees, or contract employees. KAWC has two methods by which it can present the cost structure to accomplish its work: (1) assume no vacancies and adjust overtime, temporary employee and contractor expenses accordingly; or (2) assume a vacancy rate and include increased expenses for overtime, temporary employee and contractor expenses to complete the work.[87] Here, KAWC has assumed no vacancies and adjusted overtime, temporary employee, and contractor expenses accordingly. Further, the Company only requested overtime expenses that aligned with its most recent three-year average and adjusted this figure downward by removing nonrecurring project expenses.[88] Additionally, the Company's only adjustments to its contracted services and temporary employee-related expenses reflect the costs of its acquisitions and are otherwise consistent with its 2025 actuals.[89] This approach is consistent with the Commission's ordered treatment in prior KAWC cases.[90]

In addition, KAWC's approach is also beneficial to its customers. The Company's actual experience demonstrates that its methodology avoids customers bearing additional labor costs. Between 2022 and 2026, KAWC's combined actual costs for regular labor, overtime, and contracted services have exceeded the Commission's authorized expenses.[91] This means that the risk of not recovering KAWC's labor expense is real. This fact undermines the premise of Mr. Defever's vacancy adjustment; vacancies do not necessarily produce a corresponding reduction in

[86] Prendergast Rebuttal at Exhibit RP-2R.
[87] *Id*. at 2.
[88] Prendergast Direct at 7.
[89] Prendergast Rebuttal at 20; KAWC Response to AG 2-81(b)-(c) (July 30, 2026).
[90] Case No. 2025-00122, Order at 19-20 (Ky. PSC Dec. 16, 2025).
[91] KAWC Response to PSC 3-11 (July 30, 2026); Prendergast Rebuttal at Exhibit RP-1R, Exhibit RP-2R.

the total cost of labor required to provide service. Reducing forecasted labor expense for vacancies without recognizing a corresponding adjustment for overtime and contract services expense incurred to perform the work would understate KAWC's labor expense rather than produce fair, just, and reasonable rates.[92]

Mr. Defever proposes using only part of the second methodology, recommending a vacancy rate adjustment without a corresponding adjustment to KAWC's related labor costs. Despite the Commission's favorable treatment of bilateral adjustments between staffing vacancies and other labor inputs in the Company's previous rate cases, Mr. Defever does not balance his proposed vacancy rate with a bilateral adjustment to overtime, temporary or contract labor costs.[93] A vacancy-rate adjustment would require the Company to increase its labor costs in these categories to provide service.[94] For example, KAWC is projecting 30,040 overtime hours in this case even though the Company required 36,434 overtime hours during its base period, 36,320 overtime hours in 2025, and 29,794 overtime hours in 2024.[95] Therefore, Mr. Defever's proposal to both impose a vacancy rate and reduce the Company's overtime and temporary-help expenses is unreasonable to address the costs required to perform the work.

In addition, Mr. Defever relies on a five-year average of expenses that mischaracterizes the Company's overtime costs as a fluctuating expense that is likely to decrease in the future.[96] KAWC's data demonstrates why costs associated with performing work with vacancies cannot be simply assumed to decline. Overtime expense has increased in four of the last five years and is 77 percent higher since 2021.[97] Because overtime expenses are based on employee wages, increases

[92] Prendergast Rebuttal at 4; KAWC Response to PSC 3-11.
[93] Defever Direct at 10.
[94] Prendergast Rebuttal at 11.
[95] Base Period Update Filing Exhibit 37, Schedule G, Page 3 of 10. Notably, the ratio of overtime hours to straight-time hours in all three periods was above 9.6%, whereas the Company's forecasted ratio is 7.01%.
[96] Defever Direct at 11.
[97] Prendergast Rebuttal at 9.

in wage rates further increase the cost of overtime.[98] The Company's actual experience demonstrates that a reduction to headcount utilizing a vacancy factor, like that proposed by Mr. Defever, does not warrant a corresponding assumption that the cost of overtime used to accomplish the Company's work will also decline.

***(3) Mr. Defever's adjustments overlap and constitute double counting***

As he acknowledged during cross-examination and in response to post-hearing discovery, Mr. Defever's proposed adjustments include two clear misapplications of his vacancy rate, which amount to hundreds of thousands of dollars in double counted adjustments.[99] In his testimony and at the hearing, Mr. Defever failed to justify his vacancy rate adjustments to both (1) Service Company expense, which is unaffected by Company vacancies; and (2) payroll expense as a whole, which erroneously inflates his payroll adjustments by hundreds of thousands of dollars.[100]

Mr. Defever improperly includes Service Company payroll expense in the vacancy adjustment calculation, which is specific to KAWC's historic to actual employee count.[101] Service Company charges, however, reflect the cost of work performed for KAWC by Service Company, are subject to internal review by the KAWC Director of Finance and various levels of management as they are incurred, and have been available for review in this case.[102] . In short, Service Company charges are a direct product of work incurred and have no relationship to vacancies.[103]

During cross-examination, Mr. Defever acknowledged that he did not fully understand the relationship between KAWC and the Service Company and could not identify a basis for applying

[98] *Id*. at 10-11.
[99] Oct. 14, 2026 Hearing VR (12:54:40 PM – 12:58:12 PM; 12:59:10 PM – 1:02:48 PM); Joint Intervenors response to KAWC Request Nos. PH-4-PH-11 (Oct. 30, 2026).
[100] Prendergast Rebuttal at 5, 7.
[101] *Id*. at 5-6.
[102] KAWC response to AG PH-3.
[103] Prendergast Rebuttal at 5.

KAWC's vacancy rate to Service Company expense.[104] In short, the record does not establish a relationship between Mr. Defever's proposed adjustment and the Service Company expenses included in his calculation. Without such a link, the application of a vacancy rate to Service Company expense is ungrounded and unreasonable.[105] Simply put, the Service Company expense is based on actual expenses incurred and not based on any adjustments to include vacant positions.

Second, Mr. Defever applies the 5.4% vacancy percentage to *the entirety* of KAWC's direct payroll expense while also proposing additional adjustments to overtime, performance compensation, lobbying, benefits, and payroll tax.[106] This approach ignores the impact that a vacancy adjustment would have on his other payroll adjustments and, based on calculations from Company witness Robert Prendergast, inflates Mr. Defever's adjustment by $385,974, or more than 6% of his proposed reductions to the Company's revenue requirement.[107] At the hearing, Mr. Defever "agreed in concept" with Mr. Prendergast's calculations.[108] Mr. Defever, however, did not incorporate those corrections into his errata filing. When questioned about this omission at the hearing, Mr. Defever pointed to his testimony stating that payroll adjustments "may overlap" with other adjustments.

As mentioned above, Mr. Defever's vacancy adjustment overlaps with several of his other proposed adjustments because, as identified by Mr. Prendergast in his Exhibit RP-3R and testimony, Mr. Defever begins with an all-inclusive payroll base.[109] Exhibit RP-3R applies the vacancy factor to payroll costs that include base pay, overtime, group insurance, other benefits, pension, OPEB, payroll taxes, APP, LTPP, and External Affairs costs.[110] Mr. Defever then

[104] Oct. 14, 2026 Hearing VR (12:54:40 PM – 12:58:12 PM).
[105] Prendergast Rebuttal at 6-7.
[106] *Id.* at 3.
[107] *Id.* at 6-7; Defever Direct at 5.
[108] Oct. 14, 2026 Hearing VR (12:59:10 PM – 1:01:30 PM).
[109] Prendergast Rebuttal at Exhibit RP-3R.
[110] *Id.*

proposes several separate reductions to those same costs, including overtime, benefits, payroll taxes, APP, LTPP, and External Affairs expenses.[111] The effect of applying separate adjustments to expenses already reduced through Mr. Defever's proposed vacancy adjustment therefore creates overlapping adjustments, inflating Mr. Defever's adjustments.[112] Mr. Prendergast quantified Mr. Defever's overlap, and Mr. Defever agreed in concept with Mr. Prendergast's calculations at hearing.[113] In response to post-hearing discovery, Mr. Defever again confirmed that his proposed adjustments contained, in his words "double-counting."[114]

Again, Mr. Defever did not correct the identified overlap within his errata. Although Mr. Defever generally states that payroll adjustments may overlap with others, that statement does not correct the specific overlap identified by Mr. Prendergast. The Commission's rules of procedure require that parties to a proceeding timely supplement their responses in the case if the party obtains information that indicates that the information in a response is "incorrect in any material respect."[115] The Commission has stressed that an error or omission's materiality is evaluated in relation to its potential impact on the substantive outcome of the proceeding.[116]

Here, the potential impact of Mr. Defever's overlapping adjustments is material. Although revenue requirement analysis inherently involves imperfect information and requires flexibility, because Mr. Defever's overlap materially increases Mr. Defever's proposed reductions to KAWC's revenue requirement, the Commission should evaluate those adjustments using the corrected amounts established in the record by Mr. Prendergast.

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[111] *Id.*; Joint Intervenors response to KAWC PH-4 – PH-11.
[112] Joint Intervenors' Response to KAWC Request Nos. PH-4-PH-11; Oct. 14, 2026 Hearing VR (
[113] Oct. 14, 2026 Hearing VR (1:00:48 PM – 1:01:12 PM) ("I didn't do the math, but I agree in concept, in theory.").
[114] Joint Intervenors response to KAWC PH-4 (Oct. 30, 2026). *See also* Joint Intervenors response to KAWC PH-5 – PH-11 (Oct. 30, 2026).
[115] 807 KAR 5:001 Section 4(12)(d).
[116] *An Investigation of the Accuracy of Kentucky Power's Fuel Adjustment Clause Filings*, Case No. 2016-00073, Order at 5 (Ky. PSC Jan. 18, 2017) (finding that uncorrected errors in fuel adjustment filings were not material because they were not intentional, did not impact FAC costs, and did not change customer rates).

In summary, the Company's position on including vacant roles in its forecasted labor expense is soundly supported by logic and Commission precedent. The Intervenors' position is not. It is, further, a position that has been repeatedly argued, and repeatedly denied as unreasonable. Because the Intervenors' proposal both miscalculates its adjustments and fails to recognize the basic link between a downward vacancy rate adjustment and corresponding increases in overtime, temporary help, and contracted services costs, the Commission should deny these adjustments and accept the Company's forecasted labor expenses as proposed.

***(4) The Company's Total Employee Compensation Should be Recoverable Because it is Reasonable and Prudent.***

The Company aims to offer market-level compensation that is comparable to other companies that KAWC competes with for talent to ensure that employee compensation is not only competitive, but also reasonable.[117] By using a combination of base and performance compensation, the Company satisfies the dual objectives of a competitive market-based total compensation for all employees, while continuing to motivate employees to achieve goals that will improve performance and efficiency for the benefit of the Company's customers.[118]

Employee compensation is a cost of providing utility service, like other prudently incurred costs of service recoverable in rates.[119] Employee compensation must therefore be assessed through the same lens as all other operating costs of the Company: if the compensation is prudently incurred and reasonable in amount, relative to what the industry pays for the same services, it should be recoverable through rates, not parsed out based on its individual components.[120]

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[117] Lewis Direct at 45.
[118] *Id.*
[119] *Id.* at 46.
[120] *See Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, (1944) ("[I]t is the result reached, not the method employed that is controlling."); *Ky PSC v. Commonwealth ex rel. Conway*, 324 S.W.3d 373, 383 (Ky. 2010) ("[B]ecause [KRS Chapter 278] generally recognize[s] a duty to establish 'fair, just, and reasonable rates… the *Hope* doctrine that [it is] the result reached rather than the method employed which is controlling' is applicable."). *See also*

The Company submitted a total remuneration study and an assessment of the Company's performance compensation programs through the direct testimony of Robert V. Mustich, a consultant with WTW (formerly known as Willis Towers Watson) with over thirty years of industry and compensation consulting services experience.[121] This study found that the total direct compensation (which includes base compensation and all performance compensation) that the Company provides its employees was 8 percent **below** the national market median and 5 percent **below** the regional market median.[122] It further found that total remuneration (which also includes benefits) provided by the Company was 8 percent **below** the national market median and 5 percent **below** the regional market median.[123]

Based upon these findings, none of which were disputed by the Intervenors' witness,[124] Mr. Mustich concluded that while the Company's employee compensation and total remuneration were "market competitive," which is defined as a range extending from 10 percent below to 10 percent above the market median, they fell at the low end of the competitive range from a national and regional market perspective.[125] Because the Company's total compensation and remuneration are below the national and regional market median and at the low end of the competitive range of each market, the Company's overall compensation expense is inherently reasonable and prudently incurred and should be a recoverable component of the Company's revenue requirement.[126] Although KAWC acknowledges that this cuts against recent Commission precedent on this issue, the Company believes that the Commission should consider performance-compensation

*Application of Kentucky-American Water Company for an Adjustment of Rates*, Case No. 2015-00418, Order at 5 (Ky. PSC Aug. 23, 2016) (Approving rates that, in their entirety, fall within the "range of reasonableness").
[121] Direct Testimony of Robert V. Mustich at 1 (May 15, 2026).
[122] *Id*. at 7
[123] *Id.*
[124] *See generally* Defever Direct; Oct. 14, 2026 Hearing, VR (12:35:05 PM - 1:24:55 PM).
[125] Mustich Direct at 7.
[126] Lewis Direct at 46.

holistically and recognize that the Company's approach promotes better customer outcomes while curbing overall compensation costs.

The Intervenors, through Mr. Defever, propose to remove the majority of the Company's performance-based compensation and other non-base compensation expenses from the revenue requirement.[127] Mr. Defever's vacancy adjustment separately reduces both APP and LTPP expenses by applying the vacancy percentage to those same costs, resulting in an additional reduction to expenses already subject to his proposed compensation adjustment. Therefore, to the extent those expenses are already removed through his adjustment, applying a vacancy adjustment results in a duplicative reduction, or in Mr. Defever's own words an "overlap."

The Company offers two performance-based compensation plans: the Annual Performance Plan ("APP"), which is available to all full-time employees, and the Long-Term Performance Plan ("LTPP"), which is available to certain exempt employees.[128] Under the LTPP, American Water provides restricted stock units and performance stock units as long-term performance compensation, based on three-year vesting periods.[129] The APP is designed to recognize and reward employee performance against key goals and targets that drive the Company's strategy. For example, the APP goals for 2026 focus on growth, customer satisfaction, safety, environmental compliance, system resilience, and employee engagement.[130]

Mr. Defever proposes to remove 50 percent of the Company's APP and 70 percent of the Company's LTPP from the revenue requirement, contending that as "the Company's shareholders are the primary beneficiaries of performance compensation based on financial goals, not ratepayers," they should be responsible for the costs of performance compensation tied to financial

[127] Defever Direct at 12-15.
[128] Lewis Direct at 47.
[129] *Id.* at 47.
[130] *Id.* at 48.

goals.[131] This misconception is addressed by Company witnesses William A. Lewis and Mr. Mustich, who explain that the performance-based component of the Company's total market-based compensation plan aligns the interests of KAWC customers, employees, and investors.[132] The market-based compensation philosophy that KAWC has adopted allows it to attract and retain the workforce needed to continue to provide safe and reliable service. At a time when the Company and many other employers are finding it increasingly difficult to attract and retain good employees, this point cannot be overstated.[133] Customers benefit when a utility retains talented employees, because a stable workforce avoids the costs of hiring and training new employees.[134] In particular, the Company's LTPP is intended to reduce leadership attrition.[135] Senior management turnover and the loss of expertise can degrade the continuity of strategy and execution, to the detriment of customers.[136] Importantly, the LTPP achieves its goals of reducing leadership attrition at a lower cost to customers compared to simply increasing leadership's base pay, because performance pay under the LTPP is stock-based and vests over a longer time period.[137]

In addition, the APP and LTPP compensate employees for achieving measurable goals directly tied to the delivery of clean, safe, reliable, and affordable water service and the provision of safe and reliable customer service.[138] Customers derive a direct benefit from the Company's focus on the strategic goals underlying the plans: customer satisfaction, health and safety, environmental performance, system resilience, and maintaining its skilled workforce.[139]

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[131] Defever Direct at 13; Lewis Rebuttal at 5.
[132] Lewis Direct at 54-55; Lewis Rebuttal at 5-6; Mustich Direct at 7-9.
[133] Mustich Direct at 9; Lewis Rebuttal at 10 (citing *Kentucky Water Workforce Survey*, KWRI, https://kwri.uky.edu/kentucky-water-workforce-suvey (August 2022)).
[134] Mustich Direct at 9.
[135] KAWC's response to PSC 1-27(a) (May 29, 2026).
[136] *Id.*
[137] *Id.*; Mustich Direct at 9.
[138] Lewis Direct at 54.
[139] *Id.* at 50.

Customers also benefit from the plans' well-grounded financial measures, which keep KAWC and its employees focused on improved performance at all levels, particularly in increasing efficiency, decreasing waste, and boosting overall productivity.[140]

The Commission has consistently recognized the reasonableness of compensation and benefits established through the arm's-length collective bargaining process with unionized employees. The Commission has explained that when "expense is negotiated as part of a collective bargaining agreement, the Commission has consistently allowed for the utility to recover for the full amount of an arm's length negotiated agreement with its employee union."[141] In the Company's last rate case, the Commission applied this same principle, finding that negotiated benefits received under union contracts are generally "necessary to attract and retain the employees, and therefore, that the costs are reasonable."[142]

The same rationale applies to performance compensation negotiated as part of KAWC's union contracts. APP is a component of employees' total compensation and subject to arm's-length negotiations between the Company and the union. As Mr. Mustich explained, without the APP compensation, the Company's total compensation package would no longer be market competitive regionally or nationally.[143] It follows, therefore, that the $192,706 of APP attributable to the Company's union contract, which serves to attract and retain its unionized employees, should be recoverable in rates.

Mr. Defever's proposal to remove $49,477 for the Company's Employee Stock Purchase Program ("ESPP") and $30,477 for 401(k) for the Company's remaining pension plan employees

[140] *Id*. at 55.
[141] Case No. 2025-00122, Order at 26 (Ky. PSC Dec. 16, 2025).
[142] *Electronic Application of Jackson Purchase Energy Corporation for a General Adjustment of Rates and Other General Relief*, Case No. 2024-00085, Order at 28-29 (Ky. PSC Feb. 28, 2025).
[143] Mustich Direct at 8-9.

from the revenue requirement is similarly misguided. These amounts are both included in Mr. Defever's proposed vacancy adjustment and therefore are subject to the same "overlap" or double counting issues discussed above. Like the Company's performance programs, Mr. Defever asserts that the ESPP provides no benefits to the Company's customers.[144] In fact, the ESPP is an effective tool for employee retention, and KAWC's data shows that participating employees had an average tenure of 10.7 years with the Company.[145] Similarly, removing the $30,477 used to cover 401(k) expenses related to the Company's eleven legacy pensions recipients, five of whom are union employees, would adversely affect the Company's employee retention efforts.[146]

Finally, Mr. Defever proposes an adjustment to remove $100,447 of severance expense, which represents KAWC's allocated share of Service Company costs incurred in connection with workforce restructuring. Mr. Defever describes these costs as a "generous benefit," offered by the Company.[147] However, as Mr. Prendergast explained at the hearing and in response to post-hearing discovery, the Company's severance expenses are a legitimate business expense that are limited in scope and enables KAWC and its Service Company to make restructuring decisions that support operational efficiencies.[148]

In summary, KAWC's total market-based compensation is reasonable and not excessive. It is a necessary cost incurred to serve customers, directly incentivizes practices that benefit customers, and is necessary to attract and retain skilled employees. Approving this compensation package in its totality ensures that KAWC's compensation remains market competitive and ties that compensation to real customer benefits. Given the ongoing labor shortages in the water utility

[144] Defever Direct at 16.
[145] Prendergast Rebuttal at 13.
[146] *Id.* at 14.
[147] Defever Direct at 5, 17.
[148] Prendergast Rebuttal at 18; Oct. 14, 2026 Hearing, VR (9:57:22 AM – 9:58:33 AM); KAWC response to PSC PH-23.

sector, maintaining a competitive position in the labor market is essential to achieving high-quality service. Because the Company's total employee compensation is reasonable and prudently incurred, KAWC requests that this Commission reject the Intervenors' proposals and instead include the Company's proposed total market-based employee compensation expense in the revenue requirement, which includes APP and LTPP compensation, the Employee Stock Purchase Program, and those employees who participate in a defined benefit retirement plan.

**(B) Working Capital Allowance**

Cash working capital ("CWC") is the amount of funds a utility needs available to cover its day-to-day operating expenses. For ratemaking purposes, CWC reflects the difference in the timing between when the utility pays its operating expenses for services rendered and when it actually receives revenues from its customers.[149] During this interim period, or "lag," the utility must bridge the funding gap until it receives adequate revenue to cover those expenses, which incurs financing costs.[150] The totality of this expense, CWC, is calculated by (1) measuring the utility's average materials and supplies balances to determine "Other Working Capital" and (2) conducting a lead-lag study for the specific test period.[151]

Through Mr. Defever, the Intervenors propose reducing the Company's rate base to account for cash working capital. Mr. Defever relies on the Company's 2024 lead-lag study to propose a downward adjustment to KAWC's revenue requirement.[152] Mr. Defever argues that this adjustment is necessary to remove non-cash items from KAWC's working capital calculations and,

[149] Rebuttal Testimony of John Watkins at 6 (Sep. 16, 2026).
[150] *Id.*
[151] *Id.* at 7.
[152] Defever Direct at 35.

relying on projections developed using the Company's 2024 lead-lag study, recommends reducing the Company's revenue requirement by $669,882.[153]

Mr. Defever's recommendation is flawed in concept and execution. First, Mr. Defever is recommending an adjustment to an item the Company is not seeking to recover. KAWC did not include any working capital expense in rate base and is not requesting cost recovery for CWC in this case.[154] Given the short period of time between rate cases and the variability of CWC between periods, the Company determined that declining to seek recovery for CWC in this case would avoid the additional expenses associated with a lead-lag study.[155] Because KAWC has not requested CWC in this case, the Company determined that conducting an updated lead-lag study was an unnecessary expense.[156]

The recent acquisition of Black Mountain illustrates that variability and the timing lag between the incurrence of operating expense and the recognition of CWC following an acquisition. As Mr. Watkins explained at hearing, KAWC acquired Black Mountain on October 9, 2026, without assuming the seller's receivables because Black Mountain read and billed their customer meters prior to close.[157] Immediately upon acquisition, KAWC began incurring payroll and other operating expenses necessary to serve those customers, while revenues from those customers could not be recognized until after KAWC completed its first meter-read, billing, and collection cycle.[158] That process creates an approximately 60-day lag in which KAWC incurs costs of providing service and operating the system, including four full payrolls and a partial payroll for employees,

[153] *Id*. at 34-38.
[154] Application Exhibit 37, Schedule B-5.2.
[155] KAWC's response to PSC 3-3.
[156] Application Exhibit 37, Schedule B-5.2. The Company did produce an estimate of its average materials and supplies balances, which Intervenors did not contest in their direct testimony. *See* Application Exhibit 37, Schedule B-5.1.
[157] Oct. 14, 2026 Hearing VR (10:09:56 AM – 10:10:10:12 AM).
[158] Oct. 14, 2026 Hearing VR (10:10:12 AM – 10:11:14 AM).

before it receives any corresponding revenues from Black Mountain customers.[159] This example is applicable to all acquisitions the Company makes, and Black Mountain specifically demonstrates that CWC can vary based on the timing of expenses and revenues.

Additionally, Mr. Defever's use of the Company's 2024 lead-lag study is not a reasonable basis for his proposed adjustment. As Mr. Watkins addressed in his rebuttal testimony and at the hearing, lead-lag factors approved in one case cannot be ported into another case.[160] At the hearing, Mr. Defever acknowledged that using past lead-lag studies would not provide a reliable estimate of the Company's future operations, but that he had decided to rely on the study because the Intervenors had not conducted their own lead-lag study.[161] Additionally, Mr. Defever's proposed adjustments are based on his own adjustment calculations from the prior rate case, and, as Mr. Watkins demonstrated, do not track with the Commission's CWC methodology or calculations.[162] In other words, Mr. Defever's CWC adjustment relies on both inappropriate source data and rejected methodology.

Simply put, Mr. Defever's recommendation to include a CWC component that the Company does not wish to recover is unreasonable, and his proposed adjustments to the Company's revenue requirement are ungrounded in either an appropriate lead-lag study or accepted Commission calculations. The Commission cannot reasonably rely on either his reasoning or his calculations to determine KAWC's revenue requirement. Instead, the Commission should accept the Company's proposal to leave CWC out of its revenue requirement entirely.

**(C) <u>Unaccounted-For Water</u>**

[159] *Id.*
[160] Watkins Rebuttal at 7-8, Exhibit JMW-2.
[161] Oct. 14, 2026 Hearing, VR (1:19:36 PM – 1:22:13 PM).
[162] Watkins Rebuttal at 8, Exhibit JMW-3.

In his testimony, Mr. Defever recommends a reduction of $341,582 to KAWC's production costs: purchased water, fuel and power, chemicals, and waste disposal,[163] referring to 807 KAR 5:066, Section 6(3). While the Company acknowledges that the rolling 12-month average for unaccounted-for water loss exceeds 15 percent of total water produced and purchased, the UFW percentage Mr. Defever used to calculate his adjustment includes the recently acquired Livingston and Water Service Corporation of Kentucky systems. This approach penalizes the Company for water loss conditions in those systems that predate KAWC's ownership and were inherited by KAWC through acquisitions. Applying Mr. Defever's proposed adjustment effectively penalizes the Company for conditions it did not create. More importantly, such treatment disincentivizes regionalization efforts to acquire and improve systems with existing infrastructure and water-loss challenges. KAWC should be afforded a reasonable opportunity to address inherited water loss conditions before those conditions are used to assess an adjustment to its production costs.

807 KAR 5:066, Section 6(3) establishes the permissible level of unaccounted-for water for ratemaking purposes. It provides:

> Unaccounted-for water loss. Except for purchased water rate adjustments for water districts and water associations, and rate adjustments pursuant to KRS 278.023(4), for rate making purposes a utility's unaccounted-for water loss shall not exceed fifteen (15) percent of total water produced and purchased, excluding water used by a utility in its own operations.[164]

Mr. Defever's calculation of the Company's UFW incorporates UFW percentages from the recently acquired Livingston and WSC water systems.[165] The Livingston and WSC systems' UFW figures, which were ate 75.48% and 54.76% respectively at the time his testimony was filed, reflect

[163] Defever Direct at 5, 19-21.
[164] 807 KAR 5:066 Section 6(3).
[165] Defever Direct at 20-21; Lewis Rebuttal at 14.

the maintenance and operational practices of prior ownership, not the Company's.[166] KAWC is in the process of evaluating these systems and making the necessary repairs to bring the systems' UFW down to a reasonable percentage.[167] As part of its next rate case, KAWC plans to update the Commission on its efforts to reduce the systems' UFW and address whether and to what extent the acquired systems' UFW should be included in any UFW adjustments at that time.[168] In any event, KAWC has shown that, without the acquisitions, the most recent UFW percentage is 19.05%.[169]

Approving the Company's proposed methodology will promote the purpose of the Commission's water loss regulation. In 2018, the Commission initiated Case No. 2018-00394 to investigate the effectiveness of water utilities' water loss measurement programs.[170] Finding that the purpose of the Commission's water loss regulation, 807 KAR 5:066 Section 6(3), is "to serve as an incentive to promote efficient management" due to the strong correlation between excessive water loss and the "deteriorating financial health and well-being of a jurisdictional water utility," the Commission implemented new reporting requirements.[171] Although the Commission affirmed its continued use of the 15 percent threshold, the Commission also stated it would allow a deviation if the utility demonstrates that an alternative percentage is more reasonable.[172]

In Case No. 2023-00191, the Commission denied KAWC's request for a deviation under 807 KAR 5:066 Section 6(3), finding that the Company did not demonstrate good cause for a deviation from the regulation or provide evidence identifying the proximate cause of the water loss issue.[173] Here, the Company believes that there is good cause for the Company's request and that

[166] Lewis Rebuttal at 14-15; KAWC response to PSC 4-5.
[167] Lewis Rebuttal at 15.
[168] *Id.*
[169] KAWC response to PSC PH-1
[170] *Electronic Investigation Into the Measuring, Recording, and Reporting of Water Loss by Kentucky's Jurisdictional Water Utilities*, Case No. 2018-00394, Order at 6 (Ky. PSC Nov. 22, 2019).
[171] *Id.*
[172] *Id.*at 9.
[173] Case No. 2023-00191, Order at 59-61 (Ky. PSC May 3, 2024).

the UFW records from the acquired systems are strong direct evidence of the cause of the UFW increase. Further, companies like KAWC that have the financial and technical abilities to provide safe and reliable water service should be encouraged, and not disincentivized, to acquire troubled water systems like Livingston, but with that comes their higher historical UFW. The water loss percentages in the acquired systems clearly and directly inflate the Company's water loss figures, and temporarily adjusting the Company's UFW while the Company works to resolve these water loss issues is wholly consistent with the regulation's purpose.[174]

Using the water measurements from the Company's existing system will promote efficient management. After Case No. 2023-00191, the Company made reducing water loss a priority, and its UFW percentages reflect the Company's efforts.[175] KAWC successfully reduced water loss in its existing systems for three consecutive years, going from 21.59% in 2022 to 17.56% in 2025.[176] These improvements reflect KAWC's efficient management of its system. Allowing the Company a reasonable opportunity to bring the new portions of its system into compliance would promote efficient management of the Company's systems and, therefore, there is good cause to accept the Company's proposed measurement in this case. It would also be consistent with the policy behind KRS 65.058(2) which, in the context of public water system acquisitions, requires both the Kentucky Department of Water and the Commission to grant the acquiror a forbearance period during which an acquiror shall not be required to pay any of the acquired system's fines or penalties.[177]

In conclusion, KAWC believes that any adjustment to the Company's production costs based on UFW should be calculated using the UFW percentage of KAWC's legacy systems. This

[174] Lewis Direct at 35.
[175] *Id*.
[176] *Id*. at 34-35; Lewis Rebuttal at 15; KAWC response to PSC PH-1.
[177] KRS 65.058(2).

methodology allows KAWC a reasonable period of time to identify, prioritize, and address those inherited conditions in its acquired systems. As both KAWC's figures and Mr. Defever's testimony demonstrate, the Company has reduced UFW in its existing system by roughly four percentage points and will take the same approach with its newly acquired systems. Temporarily removing the acquired systems' UFW figures from the Company's water loss percentages will aid the Company's efforts to remediate and improve water loss conditions within these inherited systems and support regionalization.[178]

**(D) Miscellaneous Expenses**

Miscellaneous expenses are a component of operating expenses that include costs related to business development, governmental and regulatory affairs, advocacy, community relations, membership dues, and directors' fees.

***(1) Membership Dues***

Mr. Defever, on behalf of the Intervenors, proposes the removal of $53,012 from reported miscellaneous expenses allocated to membership dues of $56,264, contending that those costs were for memberships in organizations that engaged in lobbying and political activities and that the Company has failed to demonstrate that the membership costs did not include costs for lobbying and political activities.[179] In fact, the only membership expenses he did not propose removing were the Company's payments to the Kentucky Department of Environmental Protection.[180] In short, Mr. Defever believes that the Company should bear all membership expenses related to any entity that engages in advocacy.[181]

[178] KAWC response to GMWSS 1-4(c) (July 30, 2026).
[179] Defever Direct at 29.
[180] *Id.* at 29-30.
[181] *Id*. at 31.

Mr. Defever's adjustment conflates the Company's community and customer engagement with lobbying. Through its membership dues to civic and regional organizations, KAWC strengthens its relationship with communities it serves and supports initiatives that strengthen local economic activity in its service territory.[182] Although these organizations engage in image building and advocacy on behalf of their regions and member communities, they do not engage in lobbying or political advocacy on behalf of KAWC. Moreover, less than a quarter of the Company's dues support these activities.[183] His adjustment therefore not only treats community and regional advocacy as if it were lobbying, but also fails to recognize the limited portion of KAWC's dues associated with those activities.

Using its three largest membership groups as a proxy, the Company was able to calculate a percentage of membership dues related to lobbying expenses of 23.1 percent and apply this percentage to its revised total 2025 Membership Dues expense of $48,006 to determine an estimated total lobbying and political activity cost of $11,097.[184]

Overall, KAWC's membership in these organizations provides benefits for its customers and their communities, which the Company has described in detail in this case.[185] While these organizations engage in lobbying activities, they are not lobbying on the Company's behalf but on behalf of their regions, their member communities, and the broader interests of Kentuckians. The Company's participation in these organizations is not for the support of lobbying provided by these organizations but to support the communities that KAWC serves and to contribute to regional initiatives that help strengthen local economic activity.[186] Furthermore, the Company's

[182] Prendergast Direct at 26.
[183] *Id*.; KAWC response to AG 1-22 (June 26, 2026).
[184] KAWC Response to AG 1-22.
[185] *Id*.
[186] Prendergast Rebuttal at 26.

participation helps ensure that KAWC remains engaged with its customers and the communities it serves and is at the forefront of local initiatives that may impact KAWC's facilities and operations.

The Commission should find Mr. Defever's proposed adjustment to disallow all membership dues is inappropriate and should instead find the dues in their entirety are reasonable costs for recovery. The benefits that these memberships provide customers and their communities, and the small portion of membership dues attributable to lobbying activities is only a fraction of total dues expense.

***(2) Service Company Business Development Expenses***

Mr. Defever proposes removing $291,898 from Service Company business development expenses, contending KAWC did not provide in detail how the Service Company's business development costs specifically benefitted Kentucky customers, and that prior Commission cases have disallowed similar costs.[187] This position ignores the many ways these expenses strengthen KAWC's relationships with businesses and community leaders in its service territory and support activities that measurably reduce the Company's per-customer costs of service.[188] As KAWC's experts testified, the Company's approach to per-customer cost management is sound, and the Company's analysis shows that its system acquisitions will only improve its per-customer cost efficiency.[189]

Company witness Robert Prendergast responded to Mr. Defever's proposal to remove Service Company business development costs allocated to the Company, explaining how these costs have facilitated reduced per-customer service costs by developing economies of scale.[190] By helping to spread system investment costs across a larger customer base, these Service Company

[187] Defever Direct at 24-25.
[188] Prendergast Rebuttal at 20-21.
[189] Direct Testimony of Joseph Weiss at 5 (May 15, 2026); Prendergast Rebuttal at 21.
[190] Prendergast Rebuttal at 21-23.

business development costs provide a demonstrable benefit to the Company's customers and are reasonable and necessary.[191] Additionally, business development supports activities that help the Company build relationships with local community leaders and businesses that can lead to better communications in emergencies, sharing of best practices, and support for local communities.[192]

Service Company business development provides for measurable benefits to KAWC customers by reducing per-customer O&M, increasing purchasing power, and supporting local economic activities within its service areas.[193] Cost mitigation occurs when business development activities allow KAWC to grow its customer base, which enables the Company to spread system investment costs and operating expenses across a larger customer group, thereby mitigating the costs to be recovered per customer.[194] The Water Service Corporation of Kentucky acquisition provides a concrete example of this benefit. As Mr. Prendergast explained, the acquisition was sourced and executed at the Service Company level and adds 5,221 customers to KAWC's customer base. The addition of those customers reduces KAWC's forecasted O&M cost per customer from $462.40 to $444.45, an approximately $18 reduction per customer.[195]

Service Company business development activities also create economies of scale that extend beyond acquired systems. A growing customer base increases American Water's purchasing power and negotiating leverage to purchase goods and services in bulk at competitive prices, benefiting KAWC and its customers.[196] These benefits enable KAWC to gain access to purchasing power and cost efficiencies associated with American Water's growing presence across its footprint, that KAWC could not otherwise achieve to the same extent on its own.

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[191] *Id*.
[192] *Id.* at 20.
[193] *Id.* at 22.
[194] *Id.* at 21-22.
[195] *Id*. at 21.
[196] *Id*.

Therefore, the benefits of Service Company business development expenses generate measurable benefits as mentioned above to the Company's customers that are not limited to acquisition activity and therefore support recovery in rates.

***(3) Board of Directors Expense***

Mr. Defever recommends that the Commission disallow 75% of the Company's Board of Directors Fees, for a total adjustment of $47,233.[197] Mr. Defever relies upon a Connecticut order he referenced in testimony and at hearing, but provided no other basis for his recommended adjustment. Mr. Defever did not identify any Kentucky precedent for his proposed adjustment and did not provide any analytical or evidentiary basis for his 75% ratio and recommended adjustment. Mr. Defever testified that his proposed adjustments were not based on his cited decisions, but were instead intended to allow proportionate recovery for the customer benefits provided by the Board of Directors.[198] However, the record does not demonstrate that Mr. Defever's disallowance was derived from an analysis of those benefits. On examination, Mr. Defever admitted that he had not reviewed *any* of the Company's Board of Directors' meeting minutes in developing his adjustment.[199] These minutes, which the Company provided at the AG's request,[200] show that the Board of Directors provide oversight and feedback that benefits its customers.[201] The Board of Directors' minutes reflect oversight and feedback regarding matters directly affecting KAWC and its customers, including KAWC's capital improvements, safety initiatives, community outreach, and the Company's H2O Help to Others program, operations, and financial matters.[202] These activities demonstrate that the Board's role specifically includes oversight and strategic planning

[197] Defever Direct at 26-27.
[198] Oct. 14, 2026 Hearing VR (1:15:50 PM – 1:17:08 PM). *See also* KAWC's response to AG 1-62.
[199] *Id*.
[200] KAWC response to AG 1-62.
[201] Prendergast Rebuttal at 25.
[202] *Id.*

specific to KAWC's operations. Through that oversight, the Board facilitates and supports KAWC's continued provision of safe, reliable service to its customers. Accordingly, the Commission should reject Mr. Defever's adjustment to Board of Directors expenses, because the Board provides oversight and strategic planning specific to KAWC's continued provision of safe and reliable service to customers. Thus, KAWC has demonstrated that the associated Board of Directors expense is reasonable and should be recovered in rates.

***(4) External Affairs Expenses***

Mr. Defever recommends an adjustment to disallow $473,472 for expenses he characterizes as lobbying, but which includes the salaries of KAWC employees involved in political advocacy, government affairs, and regulatory policy.[203] The record, however, demonstrates that these employees perform functions that extend beyond lobbying or political advocacy and directly support KAWC's utility operations and customers. These employees' responsibilities include communicating with customers and municipalities that the Company serves, responding to inquiries regarding main breaks, planned work, scheduled maintenance, and other operational matters.[204] Therefore, the identified employees' salaries cannot reasonably be treated entirely as lobbying expense and should, therefore, remain recoverable in rates.

Alternatively, if the Commission determines that some portion of these salaries should be excluded from recovery, the adjustment should be limited to the portion that is attributable to activities the Commission deems nonrecoverable. Based on the record, that would reduce Mr. Defever's adjustment from $473,472 to $275,511.

[203] Defever Direct at 28-29.
[204] Prendergast Rebuttal at 23.

The Commission should approve the Company's proposed level of miscellaneous expenses in its revenue requirement because the costs are reasonable, prudently incurred, and provide express benefits to customers.

**(E) Rate Case Expenses**

As a regulated utility, KAWC has a legal obligation to provide safe and adequate service to its customers at just and reasonable rates. Periodic rate changes are necessary to support the Company's continued provision of safe and adequate service to its customers. The way that KAWC changes its base rates is through the rate case process. The cost of litigating a rate case is a normal and essential cost of service for any regulated public utility and should be treated as such.[205]

The Company proposes to recover forecasted rate case expenses related to this case of $1,197,000 over a two-year amortization period, starting at the beginning of the forecasted test year, January 1, 2027.[206] A two-year amortization period was proposed to align with the amount of time since the Company's last rate case filing.[207] The Company further proposes to include in the forecasted test period $232,358 to reflect the amortization of the remaining balance of rate case expenses from the Company's 2025 rate case.[208] Total rate case expense included in the forecasted test period is $714,681.[209]

Intervenor witness Defever proposes to reduce forecasted rate case expense by $238,227 to reflect the use of a three-year amortization period and the amortization of $232,358 of the remaining balance of the Company's previous rate case expenses over three years.[210] This

[205] Prendergast Direct at 27.
[206] *Id.* at 18; KAWC response to PSC 1-1, W/P 3-6; KAWC response to AG 1-50.
[207] KAWC response to PSC 2-23.
[208] KAWC response to PSC 1-1, W/P 3-6.
[209] *Id.*
[210] Defever Direct at 20.

proposed adjustment should be rejected. A three-year amortization period is not consistent with the amount of time that has elapsed since the Company's last rate case filing nor is it consistent with the principle that an appropriate amortization period should reflect a utility's most recent filing history. Furthermore, extending the amortization period for the Company's unamortized 2025 rate case expenses for three *additional* years conflicts with the Commission's finding in the Company's prior rate case that a three-year amortization period was reasonable and with Mr. Defever's own testimony that a reasonable amortization period for rate case expenses is three years.[211]

On November 6, 2026, KAWC updated its actual rate case expense and that amount is $751,693.[212] Due to the timing of the regulatory process, limiting rate case expense to the actual expenses as of the closing of the record is problematic. The Company can reasonably calculate the amount of invoiced expenses almost up to the date on which the case record closes, which in this proceeding is on November 10, 2026. However, there is some level of rate case expense that must be estimated because the costs are incurred as the record closes, and *after* the record closes.

Rate case expenses, particularly legal expenses, may be incurred after the record closes for a number of reasons. After the case is submitted for a decision and the Commission issues its decision, rate case expenses could accrue for: review of the Commission's order in this case; responding to the Commission's orders related to petitions for confidential protection of sensitive information; preparing a motion for reconsideration or rehearing; briefing and reviewing intervenors' briefs on rehearing; responding to any data requests related to rehearing; or preparing and litigating an appeal through the Kentucky courts. These tasks could require input from outside

[211] Case No. 2025-00122, Order at 27-28 (Ky. PSC Dec. 16, 2026).
[212] KAWC Supplemental Response to PSC 5-7 (Nov. 6, 2026).

legal counsel and expert consultants. For these reasons, KAWC believes its total estimated rate case expense should be recovered in rates.

## IV. CAPITAL STRUCTURE

Customers benefit from a utility that is well run, generates predictable financial results, and maintains an appropriate capital structure. KAWC's customers benefit from a reasonable capital structure because it: (1) allows the Company to maintain strong credit ratings and (2) enables the Company to access capital markets on good terms and at a reasonable cost.[213] As Mr. Watkins explained in his rebuttal testimony, the Company proposes a capital structure for the forecasted test period composed of 52.29 percent common equity, 46.97 percent long-term debt, 0.45 percent short-term debt, and 0.28 percent preferred stock.[214] After adjusting projections to account for KAWC's Nexus acquisition, the Company revised its proposed capital structure to 52.24 percent common equity, 47.02 percent long-term debt, 0.45 percent short-term debt, and 0.28 percent preferred stock.[215] In light of how the Company is projected to be financed for the forecasted test year, the proposed capital structure will allow KAWC to reasonably maintain its financial strength and access cost-efficient financing so that the Company can continue providing safe and reliable service for customers. It is nearly identical to that approved in the Company's last rate proceeding and is consistent with other investor-owned utilities subject to Commission regulation.[216]

The Intervenors, through their witness Mr. Rothschild, describe KAWC's proposed capital structure as "atypically expensive," and suggest that the Commission should alter the Company's capital structure by increasing the Company's long-term debt percentage by more than 1% with a

[213] Watkins Direct at 33.
[214] *Id.* at 32, Table 3; Base Period Update Filing Exhibit 37, Schedule J-1.
[215] Watkins Rebuttal at 11.
[216] Watkins Direct at 31-33.

proportionate reduction to KAWC's common equity.[217] Mr. Rothschild supports his contention that the Company's capital structure is "atypical" by comparing its capital structure to that of its service company, American Water Company, and argues that the Company's proposal fails its obligation to, as he puts it, maintain "the lowest possible cost of capital."[218] At the hearing, Mr. Rothschild continued to rely upon his comparison between KAWC and AWC's capital structure, construing the gap as possible double leveraging or capital structure manipulation.[219]

Mr. Rothschild's arguments mischaracterize the Commission's standard for capital structure. When developing its capital structure, the Company's responsibility is more holistic than just seeking out the "lowest possible cost of capital." KAWC must develop a structure that, like its final rates, facilitates operations, maintains its financial integrity, attracts capital, and compensates its investors for risks assumed.[220] The Commission has recognized that creditworthiness is the "linchpin" of regulated utilities' financial stability, and has generally found that an acceptable capital structure maintains a balance between access to high-quality credit and low-cost debt with customer impact.[221]

KAWC's proposed capital structure achieves the appropriate balance. The Company's structure is well within the range of comparable utilities, which are the appropriate proxies for evaluating KAWC's proposed structure, and its proportion of equity is generally lower than many

[217] Direct Testimony of Aaron Rothschild at 55-56 (recommending 51.17 percent common equity, 48.09 percent long-term debt, 0.45 percent short term debt and 0.28 preferred stock) (Aug. 7, 2026).
[218] *Id.* at 55.
[219] Oct. 14, 2026 Hearing VR (12:28:51 PM – 12:29:56 PM).
[220] *See Application of Atmos Energy Corp. for an Adjustment of Rates; Approval of Tariff Revisions; & Other General Relief*, Case No. 2024-00276, Order (Ky. PSC Sep. 18, 2025) (citing *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (1944)).
[221] *Application of Big Rivers Elec. Corp. for: (1) Approval of Wholesale Tariff Additions for Big Rivers Electric Corporation, (2) Approval of Transactions, (3) Approval to Issue Evidences of Indebtedness, and (4) Approval of Amendments to Contracts; and of E.ON U.S., LLC, Western Kentucky Energy Corp. and LG&E Marketing, Inc. for Approval of Transactions*, Case No. 2007-00455, Order at 37-39 (Ky. PSC Mar. 6, 2009).

of its peers and, after the adjustment discussed by Mr. Watkins on rebuttal, is slightly lower than the equity ratio approved in the Commission's 2025 order.[222]

Mr. Rothschild's concerns about capital structure manipulation are unsubstantiated because the difference between KAWC's and American Water's capital structures do not, standing alone, establish capital structure manipulation or double leveraging. Because the Commission is relying on a proxy group of companies to determine the cost of equity for KAWC, it is important that the financial risk of KAWC be similar to the proxy group; therefore the appropriate benchmark for KAWC's equity ratio is the proxy group and not the parent company, American Water's capital structure. Further, Mr. Rothschild's comparison of the Company's proposed equity ratio to the equity ratios of the proxy group companies at the holding company level is inappropriate because as KAWC witness Bulkley observed, the capital structures of holding companies fundamentally differ from regulated utilities.[223] Mr. Rothschild's comparison also relies on the book value of debt and equity for the proxy group companies at the holding company level; however, the use of the book value of debt and equity creates a mismatch between the capital structure data that is being used to determine the reasonableness of KAWC's equity ratio and the data that is being used in the models to determine the cost of equity for KAWC.[224] When KAWC's equity ratio is evaluated against the market value of these holding companies, KAWC's equity ratio is actually *lower* than Mr. Rothschild's proxy holding companies.[225] Finally, KAWC notes that capital structure manipulation is a serious claim that the Commission has not taken lightly, and that a

[222] *Compare* Watkins Rebuttal at 10-11 *with* Case No. 2025-00122, Order at 49 (Ky. PSC Dec. 15, 2026).
[223] Rebuttal Testimony of Ann E. Bulkley at 70-71 (Sep. 16, 2026).
[224] *Id.* at 71-73.
[225] *Id.* at 71-73.

reasonable difference between capital structures is not evidence of "double-leveraging."[226] Therefore, solely because a difference exists, Mr. Rothschild has not established that KAWC's capital structure has been manipulated or that its equity ratio results from double leveraging.

## V. COST OF EQUITY AND RATE OF RETURN

The key to determining a reasonable rate of return on equity ("ROE") is to ensure that the analysis reasonably reflects investors' views of the financial markets—both in general and, in the context of a proxy group, of the subject company. The Company's ROE recommendation draws from multiple analytical techniques that rely on market-based data to quantify investor expectations regarding required equity returns, adjusted for certain incremental costs and risks. Quantitative models produce a range of reasonable results from which the market-required ROE is selected. That selection is based on a comprehensive review of relevant data and information and does not necessarily lend itself to a strict mathematical solution.

KAWC retained an expert, Ann E. Bulkley, to conduct thorough, independent, market-based cost of equity analyses to recommend a reasonable ROE. The differences in the recommended ROEs sponsored by the parties in this case are significant. The Company recommends a ROE of 10.75 percent.[227] Meanwhile, the Intervenors, through their expert, Aaron Rothschild, recommend a ROE of 8.07 percent, which falls well below the 10.25 percent to 11.25 percent range recommended by Bulkley. When reasonable adjustments are made to address the issues identified with Mr. Rothschild's cost of equity analyses, the results of his models significantly increase and support the Company's proposed ROE in this proceeding.[228]

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[226] *See Electronic. Application of Bluegrass Water Utility. Operating Co., LLC for an Adjustment of Sewage Rates*, Case No. 2022-00432, Order (Ky. PSC June 29, 2023) (addressing Attorney General's allegation that utility was engaging in capital structure manipulation based on classification of debts as "Liabilities Payable to Associated Companies").
[227] Direct Testimony of Ann E. Bulkley at 5 (May 15, 2026).
[228] Bulkley Rebuttal at 7.

**(A) Framework for Determining a Fair and Reasonable Cost of Equity**

The United States Supreme Court's *Hope*[229] and *Bluefield*[230] decisions established the standards for determining the fairness and reasonableness of a utility's authorized ROE. Among the standards established by the Court in those cases are: (1) consistency with other businesses having similar or comparable risks; (2) adequacy of the return to support credit quality and access to capital; and (3) the principle that the specific means of arriving at a fair return are not important, only that the end result leads to just and reasonable rates.[231] In the oft-cited *Hope* decision, the United States Supreme Court stated:

> From the investor or company point of view, it is important that there be enough revenue not only for operating expenses, but also for the capital costs of the business. These include service on the debt and dividends on the stock. By that standard, the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.[232]

In following *Hope* and *Bluefield*, the Commission's order in this proceeding should establish rates that provide the Company with a reasonable opportunity to earn a ROE that is: (1) adequate to attract capital at reasonable terms; (2) sufficient to ensure its financial integrity; and (3) commensurate with returns on investments in enterprises with similar risks.[233]

It is important to recognize that investors make rational decisions regarding investments of comparable risk. If an investment does not receive a comparable return to other investments of similar risk, it will be difficult to attract capital.[234] Because investors are likely to invest equity in

[229] *Fed. Power Comm'n v. Hope Nat. Gas Co.*, 320 U.S. 591 (1944).
[230] *Bluefield Water Works & Improvement Co. v. Public Serv. Comm'n*, 262 U.S. 679 (1923).
[231] Bulkley Direct at 5.
[232] *Fed. Power Comm'n v. Hope Nat. Gas Co.*, 320 U.S. 591, 603 (1944) (internal citations omitted).
[233] Bulkley Direct at 9.
[234] *Id.* at 9-10.

utilities with the highest returns, authorizing a return for KAWC that is below the returns awarded to other water, natural gas, and electric utilities could negatively affect the Company's access to capital over the long-term.[235] An authorized return on equity for KAWC that fails to account for the financial risks on cash flow metrics and is substantially below the returns of other risk-comparable utilities would disadvantage KAWC and its customers.

**(B) <u>The Company's Proposal</u>**

***(1) KAWC's Recommended ROE is Reasonable and Supported by Substantial Evidence.***

Ms. Bulkley's analyses incorporate several equity estimation methods, including the Constant Growth Form of the Discounted Cash Flow ("DCF") model, the Capital Asset Pricing Model ("CAPM"), and the Empirical Capital Asset Pricing Model ("ECAPM") to a proxy group of comparable-risk utility companies.[236] She also considered the Company's business and regulatory risk as compared with the proxy group, which included a comparison of capital expenditure requirements and adjustment mechanisms.[237] In addition, Ms. Bulkley's analyses considered capital market conditions and demonstrated that (1) the inflation rate remains elevated;[238] (2) significant policy changes (i.e., trade, immigration, fiscal policy, and regulation) by the Trump administration have increased uncertainty regarding the path of monetary policy; (3) the Fed is again raising interest rates due to inflation continuing to remain above the Fed's target of 2 percent; and (4) long-term interest rates are expected to continue to remain elevated during the period that the Company's adjusted rates will be in effect.[239] The changes in capital market conditions since the Commission's decision in the Company's last rate case indicate that KAWC's

[235] *Id.* at 7.
[236] *Id.* at 17-19.
[237] *Id.* at 36-45.
[238] Bulkley Rebuttal at 56.
[239] *Id.* at 9-10.

cost of equity and ROE should be higher than what was approved in the Company's previous rate case—not significantly lower, as proposed by the AG.

Ms. Bulkley established a proxy group of companies that are both publicly traded and comparable to KAWC in certain fundamental business and financial respects to serve as a "proxy" for purposes of the cost of equity estimation process.[240] The proxy companies all possess a set of operating and financial risk characteristics that are substantially comparable to KAWC, and therefore provide a reasonable basis for deriving the appropriate ROE.[241] Ms. Bulkley developed the proxy group by first identifying U.S. utilities that Value Line classifies as water utilities and natural gas distribution companies applying certain screening criteria.[242] Because of the trend towards consolidation in the utility industry and the resulting small number of water utility companies available for inclusion in the proxy group, Ms. Bulkley considered natural gas distribution companies.[243] After applying the screening criteria for these companies, the final proxy group comprised eleven publicly traded water and natural gas utilities that operate across the United States.[244] The reasonableness of the proxy group is not contested as the AG's witness relied upon the same proxy group, contending that the group "provide[s] a reasonable basis to derive and estimate the appropriate cost of equity" for KAWC in this proceeding.[245]

Ms. Bulkley first applied the Constant Growth DCF model. The DCF method is premised on the assumption that a stock's current price represents the present value of all expected future cash flows.[246] The Constant Growth DCF model requires the following assumptions: (1) a constant growth rate for earnings and dividends; (2) a stable dividend payout ratio; (3) a constant price-to-

[240] Bulkley Direct at 18.
[241] *Id.*
[242] *Id.* at 18-19.
[243] *Id.* at 19.
[244] *Id.* at 24.
[245] *Id.* at 18.
[246] *Id.* at 28.

earnings ("P/E") ratio; and (4) a discount rate greater than the expected growth rate.[247] For the proxy group, the mean and median Constant Growth DCF results using the average growth rates range from 10.62 percent to 11.14 percent and the mean and median results using the maximum growth rates are in the range of 11.54 percent to 12.04 percent.[248]

Ms. Bulkley also performed a traditional CAPM method of estimating the cost of equity, which is a risk premium approach that estimates the cost of equity for a given security as a function of a risk-free return plus a risk premium to compensate investors for the non-diversifiable or "systematic" risk of that security.[249] To estimate her risk-free rate, Ms. Bulkley used (1) the current 30-day average yield of 30-year U.S. Treasury bonds; (2) the average projected 30-year U.S. Treasury bond yield for the second quarter of 2026 through the second quarter of 2027; and (3) the average projected 30-year U.S. Treasury bond yield for 2027 through 2031.[250] Bulkley used the average Beta coefficients for the proxy group companies as reported by Value Line, as well as a long-term average utility beta coefficient calculated as an average of the Value Line beta coefficients for the proxy group companies from 2013 through 2025.[251] She estimated the Market Risk Premium based on the expected total return on the S&P 500 Index less the 30-year Treasury bond yield.[252] Ms. Bulkley obtained a range of traditional CAPM results for the proxy group of 10.90 percent to 11.20 percent.[253]

In addition, Ms. Bulkley performed an ECAPM—the empirical form of the CAPM—which addresses the tendency of the traditional CAPM to underestimate the cost of equity for companies

[247] *Id.*
[248] *Id.* at 31.
[249] *Id.* at 31-32.
[250] *Id.* at 32.
[251] *Id.* at 33.
[252] *Id.* at 32.
[253] *Id.* at 36.

with low beta coefficients, such as regulated utilities.[254] The ECAPM analysis first calculates the product of the adjusted beta coefficient and the market risk premium and applies a weight of 75.00 percent to that result, then calculates the market risk premium without any effect from the beta coefficient and applies a 25.00 percent weight to that result.[255] The combined results of the two calculations, along with the risk-free rate, produce the ECAPM result.[256] Ms. Bulkley obtained a range of ECAPM results for the proxy group of 11.42 percent to 11.65 percent.[257]

After performing these analyses, Ms. Bulkley then considered several factors that would affect the Company's risk profile relative to the proxy group. These included the Company's projected capital expenditure requirements and the regulatory environment in which it operated. She found that KAWC's capital expenditure requirements as a percentage of net utility plant are significant, and that, without an approved tracking mechanism for these expenditures, the Company's risk regarding timely recovery of these capital expenditures would be higher than the proxy groups'.[258] She further found that the Company had greater than average regulatory risk as compared to the proxy group as the other members of the group have more timely cost recovery between rate proceedings and the Company had significantly under-earned its authorized ROE in nine of the last eleven years.[259]

Ms. Bulkley's research and analysis demonstrates that the 10.75 percent ROE is reasonable for the Company's base rates *and* the proposed SIP mechanism. The appropriate comparison for purposes of assessing the business risk and regulatory risk of the Company is relative to the operating utilities of the proxy group – not focusing solely on the Company. As shown on Exhibit

[254] *Id.* at 34.
[255] *Id.*
[256] *Id.*
[257] *Id.* at 35.
[258] *Id.* at 40.
[259] *Id.* at 44-45.

AEB-8 in Ms. Bulkley's Direct Testimony, the vast majority of the operating subsidiaries of the proxy group companies have mechanisms to recover the cost of capital expenditures outside of rate proceedings. If the SIP mechanism is approved at a reduced ROE, the Company is mistakenly being treated as *less* risky than the proxy group, which Ms. Bulkley's detailed analysis clearly refutes.[260]

In summary, Ms. Bulkley found a reasonable range for KAWC's ROE in this proceeding is from 10.25 percent to 11.25 percent, and within that range, an ROE of 10.75 percent reasonably reflects investor-required return. Her recommendation is based upon detailed cost of equity analyses and consideration of the business and regulatory risks that the Company faces, is supported by significant evidence, reflects current and expected economic conditions, and should be adopted.

**(C) <u>The Intervenors' Proposal</u>**

***(1) The Intervenors' Estimated Cost of Equity Fails to Reflect That the Cost of Equity Has Increased Since the Company's Last Rate Proceeding.***

The AG filed direct testimony regarding KAWC's return on equity through its witness, Mr. Rothschild. Mr. Rothschild reached his recommendation after performing DCF and CAPM analyses, using Ms. Bulkley's selected proxy group and a second proxy group of four water utilities, and relying primarily on a constant growth DCF model, non-constant growth DCF model and a CAPM Model.[261] In explaining his analysis, Mr. Rothschild argued that his DCF approach is grounded in current capital market data. Although the median result of Mr. Rothschild's modeling was 6.93%, he relied on the 80$^{th}$ and 90$^{th}$ percentile of his results to set his recommended

[260] Bulkley Rebuttal at 67-68.
[261] Rothschild Direct at 19; Bulkley Rebuttal at 34-36.

ROE range of 7.95 percent to 9.11 percent and recommended an ROE of 8.07 percent for KAWC, which was the 85th percentile of his cost of equity results.[262]

Mr. Rothschild's ROE recommendation should be rejected because it uses flawed methodology, is directionally inconsistent with current capital market conditions, and fails to reflect that the cost of equity has increased since the Company's last rate proceeding. As Ms. Bulkley addressed, many of Mr. Rothschild's findings actually align closely with the Company's when adjusted to rely on appropriate inputs.[263]

In the Company's last rate proceeding, the Commission approved a ROE of 9.70 percent. Mr. Rothschild's recommended ROE of 8.07 percent is 163 basis points below the Company's currently authorized ROE.[264] Between the Commission's decision in KAWC's 2025 rate proceeding and the hearing in this case, long-term interest rates have risen. Specifically, the 30-year Treasury bond yield increased 31 basis points between the Commission's decision in KAWC's 2025 rate proceeding and July 31, 2026 (i.e., the end of the analytical period relied on in Ms. Bulkley's rebuttal testimony).[265] During examination, Mr. Rothschild acknowledged that the 10-year Treasury yield rose approximately 110 basis points—from about 4.1 percent to roughly 5.2 percent—between the December 2025 decision and the hearing; that the 10-year yield reached its highest level in 24 years the week before the hearing; that the 30-year Treasury yield rose approximately 90 basis points over the same period; and that the Federal Reserve raised interest rates in September 2026.[266] Because there is a positive relationship between bond yields and the investor-required return on equity, a recommendation to set the Company's ROE well below its

[262] Rothschild Direct at 7-8.
[263] Bulkley Rebuttal at 64.
[264] *Id.* at 5, 10.
[265] *Id.* at 9-10.
[266] Oct. 14, 2026 Hearing VR (12:08:18 PM – 12:11:50 PM).

currently authorized level is inconsistent with reasonable investor expectations in the current market.[267]

Mr. Rothschild's own analysis demonstrates that his recommendation is not informed by the results of his cost of equity models. A strict application of his methodology would point to the 50th percentile (median) of his results, which is 6.93 percent.[268] Rather than recommend that result, Mr. Rothschild relied on what he described as the "regulatory principle of gradualism" and instead selected the 80th-to-90th percentile of his model results as a "measured, transitionary" recommendation during a purported "market correction."[269] Mr. Rothschild's recommendation is ultimately based on a discretionary upward adjustment from his model results. Even after this adjustment, his recommendation remains 163 basis points below KAWC's last authorized ROE. This difference warrants consideration of whether Mr. Rothschild's underlying assumptions and results produce a reasonable measure of the cost of equity.

Further, the results on which Mr. Rothschild relies are inconsistent with the standards prescribed in *Hope* and *Bluefield*. Although Mr. Rothschild concedes that the United States Supreme Court's decisions in *Hope* and *Bluefield* require a return commensurate with returns on investments in enterprises having corresponding risks,[270] the bulk of his model results fall below any authorized ROE for water, natural gas, or electric utilities since at least 2010.[271] His CAPM results for the Combination Proxy Group range from 5.32 percent to 7.22 percent, and his option-implied DCF and non-constant DCF results for the Combination Proxy Group range from 6.78 percent to 7.99 percent—returns that do not provide a sufficient equity premium above the

[267] Bulkley Rebuttal at 11-12.
[268] Rothschild Direct at 10.
[269] *Id*.
[270] *Id*. at 4, 17.
[271] Bulkley Rebuttal at 13–14.

Company's 4.84 percent cost of debt to be credible estimates of the investor-required return on equity.[272] Returns of that magnitude do not satisfy the comparable-return standard that *Hope* and *Bluefield* require.[273]

In her rebuttal testimony, Ms. Bulkley identified several flaws in each of Mr. Rothschild's models. Mr. Rothschild's constant growth DCF relies on a "sustainable growth" rate that assumes a positive relationship between earnings retention and future earnings growth, whereas studies consistently demonstrate a *negative* relationship between retention ratios and earnings growth.[274] When Mr. Rothschild's sustainable growth rate is replaced with the average projected earnings growth rates from Value Line, S&P, and Zacks, the cost of equity range for his Combination Proxy Group becomes 11.36 percent to 11.44 percent, and the cost of equity range for his Water Proxy Group becomes 10.56 percent to 10.81 percent.[275]

The Commission should also disregard Mr. Rothschild's constant growth DCF model that relies on option implied growth rates because his option implied growth rates: (1) lack academic support; (2) are based on limited options contract data for utilities, which results in Mr. Rothschild being unable to estimate options implied growth for significant periods of time; (3) are based on created data for periods where options data is not available; (4) have significant variability depending on the expiration date of the options contract used; and (5) have significant variability from week to week.[276] At the hearing, Mr. Rothschild admitted that he could not calculate an option-implied growth rate for many companies in his proxy group for numerous weeks—including no rate at all for Northwest Natural Gas for the entire fourteen-week period, and no

[272] *Id.* at 5.
[273] *Id.* at 6.
[274] *Id.* at 13, 25-26.
[275] *Id.* at 33-34, Exhibit AEB-8-R.
[276] *Id.* at 27-32.

growth rate for three of the four water utilities for roughly nine weeks—and that, where data were missing, he filled the gaps by interpolating between observations, carrying the last observation forward, and back casting later observations.[277] He conceded that the "resulting data series is not comprised solely of market data,"[278] and that his option-implied growth rates are sensitive to the expiration date he selects. For example, for H2O America, Mr. Rothschild's own data produced a negative growth rate of -1.38 percent for a 3.6-month option—a result he chose not to use.[279] A methodology that depends on fabricated inputs and has significant variability cannot be relied upon to set rates.[280]

Additionally, Mr. Rothschild argues that Ms. Bulkley's 10.75 percent recommendation is not "market-based" and rests on "biased" analyst forecasts.[281] However, Mr. Rothschild's non-constant growth DCF depends entirely on Value Line analyst projections.[282] That reliance is difficult to reconcile with Mr. Rothschild's criticism of Ms. Bulkley's use of analyst projections in her analysis, particularly because analyst projections are an input within his non-constant growth DCF model. Further, the use of a non-constant growth DCF model requires a number of subjective assumptions such as the specification of the model (i.e., two-stage or three-stage DCF model), the selection of growth rates, and the duration of each stage of growth in the DCF model, which results in a greater opportunity for an analyst to influence the results of the DCF model.[283] Notably, in a 2022 Pennsylvania-American Water proceeding, Mr. Rothschild declined to rely on his own non-constant growth DCF, explaining that it "could understate" the utility's cost of equity.[284]

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[277] Oct. 14, 2026 Hearing VR (12:17:10 PM – 12:17:33 PM).
[278] Oct. 14, 2026 Hearing VR (12:25:10 PM – 12:26:10 PM
[279] Oct. 14, 2026 Hearing VR (12:26:28 PM – 12:27:43 PM); Bulkley Rebuttal at 30–31.
[280] Bulkley Rebuttal at 48–51.
[281] Rothschild Direct at 56-58.
[282] Bulkley Rebuttal at 35–36; Rothschild Direct at 29–30.
[283] Bulkley Rebuttal at 34.
[284] *Id*. at 35.

Mr. Rothschild's CAPM analyses utilizes the yield on 3-month Treasury bills as well as the yield on the 30-year Treasury bonds as the estimates of the risk-free rate. However, Mr. Rothschild's use of the yield on 3-month Treasury bills is inappropriate for valuing the long-lived assets of a utility; Ms. Bulkley notes the 30-year Treasury yield is the appropriate measure.[285] Mr. Rothchild relies on a "forward beta" which is based on options contracts and a "historical blended beta" which is based on a weighted average of his 6-month, 2-year and 5-year historical beta with primary weight placed on the 6-month historical betas.[286] His "forward betas" rely on the same limited options data utilized in his DCF. Mr. Rothschild's "historical blended betas" can be affected by market dislocations because he has placed primary weight on the 6-month historical betas and therefore, his "historical blended betas" can vary significantly from week to week.[287] Mr. Rothschild also relies on the use of options contracts to calculate his market risk premium; therefore, his market risk premium suffers from the same flaws as his forward betas and options implied growth rates in his DCF. Further, those options contracts, which represent options investors' predictions as to the direction of the market over the near-term, could be incorrect. Ms. Bulkley notes that options buyers lose 90 percent of the time, which is worse than the average patron at a casino.[288] When Mr. Rothschild's CAPM is corrected to use the 30-year Treasury yield, his own five-year historical betas, and a current forward-looking market return, his CAPM results increase from a range of 5.61 percent to 7.22 percent to approximately 10.36 percent to 10.37 percent for his Combination Proxy Group and from a range of 5.16 percent to 7.44 percent to 10.31 percent to 10.33 percent for his Water Proxy Group.[289]

[285] Bulkley Rebuttal at 36–37.
[286] *Id*. at 36, 39-40.
[287] *Id*. at 39-40.
[288] *Id*. at 46.
[289] *Id*. at 57.

In other words, when corrected for the flaws Ms. Bulkley identified, Mr. Rothschild's own DCF and CAPM analyses support the Company's requested ROE.[290]

## VI. UNCONTESTED ISSUES

### (A) Uncontested Rate Base Issues

Rate base measures the Company's net investment in the provision of water service.[291] This investment includes the facilities and property for sourcing, treating, pumping, and distributing potable water for consumption, sanitation, and fire protection, as well as assets to support customer account, customer service, and basic business operations.[292] Of the rate base components included in the Base Period Update Exhibit 37 Schedule B-1, the only contested component of the Company's proposed rate base, as previously discussed, is the working capital allowance. All other rate base components are reasonable as proposed by the Company and should be approved.

The Company's methodology for calculating rate base utilizes a thirteen-month average rate base calculation for the forecasted test year.[293] Most of the rate base elements were forecasted from actual per books data as of February 28, 2026, adjusted for changes expected through December 31, 2027.[294]

#### *(1) Construction Work in Progress and Allowance for Funds Used During Construction*

In prior rate cases, KAWC has included Construction Work in Progress ("CWIP") in rate base and has calculated the Allowance of Funds used During Construction ("AFUDC") based on the CWIP-eligible balances. The present rate and forecasted revenues were then reduced by this

[290] *Id.*at 64–66.
[291] Watkins Direct at 10.
[292] *Id.*
[293] *Id.* at 5-6.
[294] *Id.*

AFUDC amount. While it had previously approved this practice,[295] the Commission ordered that CWIP be removed from KAWC's rate base in Case No. 2023-00191.[296] To comply with the Commission's order, the Company has excluded CWIP balance from rate base, removed the AFUDC, and adjusted amortization expense to align the forecast for amortized property losses and AFUDC.[297]

***(2) Additional Uncontested Rate Base Components***

Several additional components of the Company's proposed rate base[298] have been uncontested in this proceeding, namely: Utility Plant in Service ("UPIS"),[299] Utility Plant Acquisition Adjustments ("UPAA"),[300] Accumulated Depreciation,[301] Material and Supplies, Contributions in Aid of Construction ("CIAC"),[302] Deferred Income Taxes,[303] Deferred Income Tax Credits,[304] Deferred Maintenance,[305] Deferred Debits,[306] and Customer Advances.[307] The Company made no adjustments or revisions to the proposed amounts of these uncontested components throughout the pendency of this proceeding.[308]

**(B) <u>Other Uncontested Issues</u>**

***(1) Hydrant Fees***

As part of its proposed rate adjustment, KAWC proposed reducing its monthly public fire hydrant fees from $75 per hydrant to $11.53 per hydrant. Although Commission staff addressed

[295] Case No. 2010-00036, Order at 12 (Ky. PSC Dec. 14, 2010).
[296] Case No. 2023-00191, Order at 12 (Ky. PSC May 3, 2024).
[297] Watkins Direct at 27; Base Period Update Filing Exhibit 37, Schedule C-1.
[298] *See* Base Period Update Filing Exhibit 37, Schedule B-1, Page 2 of 2.
[299] Watkins Direct at 12.
[300] *Id.*
[301] *Id.* at 12-13.
[302] *Id.* at 13.
[303] *Id.* at 14.
[304] *Id.* at 16.
[305] *Id.* at 11-12.
[306] *Id.* at 13.
[307] *Id.* at 14.
[308] *Compare* Application at Exhibit 37, Schedule B-1 *with* Base Period Update Filing Exhibit 37, Schedule B-1.

the Company's proposed reduction to public hydrant fees in discovery, none of the Intervenors contested the Company's proposal at the hearing or in their direct testimony.[309]

At the hearing, KAWC witness William Lewis explained that the Company's proposal was a reasonable adjustment designed to accommodate the financial conditions of municipalities while ensuring cost recovery for the actual costs of maintaining public hydrants on the Company's system.[310] Additionally, sharing these hydrant costs will support fire safety in communities across the Company's footprint.[311] Finally, KAWC witness Charles Rea explained his cost-of-service calculations for the $11.53 proposed hydrant fee, which, again, have not been contested.[312]

The Commission should approve KAWC's proposed adjustment to its hydrant fees because it is consistent with existing practices among Kentucky water utilities, will facilitate regionalization, and is supported by a reasonable cost of service approach.

***(2) System Acquisition Expense and Net Acquisition Accounting***

On October 9, 2026, the Company closed its acquisition of the Black Mountain water system.[313] Together, the rate base impact of the WSC, Livingston and Black Mountain Systems total $1.8 million.[314] Although Intervenors raised general concerns about equitable cost sharing between existing and new customers and water system regionalization, no party has argued that recovering the direct costs of system acquisitions is inappropriate.

Pursuant to KRS 278.295(4), the Company has requested permission to establish the values of the Black Mountain water system using net acquisition accounting ("NAA") and, if this request is approved, will adjust its valuation figures in Case No. 2026-00097 to reflect the system's NAA

[309] *But see* Oct. 13, 2026 Hearing VR (3:50:00 PM – 3:52:55 PM) (cross-examination of Mr. Rea regarding the possible consequences of embedding fire hydrant fees in rates).
[310] Lewis Direct at 36-37; Oct. 13, 2026 Hearing VR (1:30:12 PM – 1:31:51 PM).
[311] KAWC response to GMWSS 1-4(a).
[312] Direct Testimony of Charles Rea at 33-36 (May 15, 2026); KAWC response to PSC 2-17, 2-18, 2-22.
[313] Case No. 2026-00097, Kentucky-American Water Company's Closing Report (Ky. PSC Oct. 9, 2026).
[314] Watkins Rebuttal at 5.

valuation.[315] NAA is a GAAP standard approach that measures the identifiable assets acquired, the liabilities assumed and any noncontrolling interests at their acquisition-date fair values.[316] Because NAA uses the acquisition-date fair value, it reflects the depreciation to date and the asset's remaining service potential.[317] NAA therefore reflects the age, wear and tear, and remaining useful life of the acquired systems.[318] As Mr. Watkins explained in his direct testimony, using Original Cost Accounting is expected to cost customers $185,833 per year, whereas NAA accounting, because it reflects the factors above, would yield costs of $29,702 per year.[319] The Commission should approve the Company's request because the proposed accounting is an accepted accounting principle treated as best practice by major accounting firms, and will yield customer savings of approximately $156,000 per year.[320] If the Commission rejects this proposal, it will need to increase the depreciation expense amount by $156,131 and the flow through effects of the higher depreciation expense.

## VII. KAWC CUSTOMER ISSUES

Both GMWSS and LFUCG raised issues throughout this proceeding that fall outside the scope of a rate adjustment case, and that the Company believes can and should be addressed and resolved outside of this proceeding.

### (A) GMWSS Issues

Throughout this case, GMWSS and its representatives raised concerns about the Company's alleged misapplication of KRS 278.030 and KRS 278.170, the filing status of a service contract executed 27 years ago, alleged special treatment of a handful of Sales for Resale

[315] Watkins Direct at 22-26; KAWC response to AG 2-47(3).
[316] *Id*. at 23.
[317] *Id*. at 24.
[318] *Id*.
[319] *Id*. at 25.
[320] *Id*. at 24-25.

customers, unfair cost allocations, and the alleged detrimental effects that KAWC's system acquisitions have on regionalization. This brief and the record in this case have adequately addressed most of these issues. Although the Company believes that GMWSS's remaining critiques are better suited for a separate discussion between KAWC and GMWSS, the Company will briefly address them here.

GMWSS's participation in the case can be distilled into a single issue: GMWSS believes that the Company's Sales for Resale rate is too high, and it would like to pay a different one. The problem is that GMWSS cannot change its rate classification by misreading Kentucky law and has ignored the Company's good faith efforts to discuss a mutually beneficial solution.

***(1) GMWSS's 2026 Purchase Volumes***

GMWSS points to its high-volume purchases between February-March 2026 to argue that the Company's Sales for Resale rates are unduly volatile and that the increase in rates between 2025 and 2026 created budgeting challenges for customers like GMWSS.[321] Although Sales for Resale rates did increase from February 2025 to February 2026, the volatility in GMWSS's water bills was the result of GMWSS's own drastic increase in consumption from one year to another. In February and March of 2026, GMWSS purchased more than 51 million gallons of water at its Champion Way interconnection – more than twenty times the amount it purchased from the Company in 2025.[322] Without providing written notice to anyone in KAWC's leadership, GMWSS took its Royal Spring plant offline for facilities upgrades and made up the difference with bulk purchases from KAWC and the Frankfort Plant Board.[323]

[321] Direct Testimony of Chase Azevedo at 11 (Aug. 7, 2026).
[322] Affidavit of Azevedo Affidavit at ¶¶ 4-7.
[323] William Lewis Rebuttal at 17; GMWSS response to KAWC 1-6 (Sep. 10, 2026).

KAWC did not include GMWSS's 51-million-gallon purchase in its Forecasted Test Year because it is not likely to occur again, and was an aberration from GMWSS's recent usage.[324] Additionally, GMWSS acknowledged that the project was the first of its kind since 2018,[325] and that it was not planning to purchase water from KAWC at that scale in the near future. At the hearing, Mr. Azevedo confirmed that GMWSS does not anticipate taking its Royal Spring plant offline for more than three days at any point in 2027.[326] In other words, GMWSS's high 2026 usage was an aberration that should not have any bearing on the Commission's ratemaking decisions in this case.

***(2) Sales for Resale Class***

Separately, GMWSS argued that it should not be a Sales for Resale customer *at all*. In written responses to Commission data requests and at the hearing, GMWSS board member and witness Kent Chandler argued that GMWSS's Champion Way should not be classified as a Sales for Resale account because the definition of "Sales for Resale customer" in the Company's tariff is too narrow and does not address all of the factors in KRS 278.030(3).[327] Because GMWSS's Champion Way account is not a year-round customer, he argues that the sale for resale classification fails to account for "the nature of the use, the quantity used, the quality used, and the time when used," which are all factors a utility may consider when developing customer classes under KRS 278.030(3).[328] Later, GMWSS addressed the gap between the general sale for resale rate and the special contracts between KAWC and two sale for resale customers, Harrison County and Nicholas County, which the Company assumed upon acquiring the City of Millersburg's

[324] KAWC response to AG PH-9(g).
[325] GMWSS response to KAWC 1-5 (Sep. 10, 2026).
[326] Oct. 14, 2026 Hearing VR (11:24:40 AM – 11:25:55 AM).
[327] GMWSS response to PSC 1-2(e); Oct. 13, 2026 Hearing VR (2:11:25 PM – 2:14:01 PM). *See* Tariff of Kentucky-American Water Company at Original Sheet No. 4 (Effective December 16, 2025) ("1.9 Sales for Resale or 'Resale' – Sales to private or public water utilities where the water is to be resold to customers of the utilities.").
[328] GMWSS response to PSC 1-2(e) (Sep. 10, 2026).

system. Throughout the cross-examination of Mr. Rea, GMWSS suggested that these contracts either demonstrate the reasonableness of the Company's Sales for Resale rates or inappropriately increase costs for the Company's other Sales for Resale customers.[329]

GMWSS rate classification argument misrepresents the plain language of KRS 278.030(3). The statute does not require utilities to weigh any particular factor when developing classifications; it merely states that as utilities develop "suitable and reasonable classifications" of service, they ***may*** consider the "nature of the use, the quality used, the quantity used, the time when used, the purpose for which used, **and any other reasonable consideration**."[330] Kentucky courts have interpreted KRS 278.030(3), together with KRS 278.170 as offering utilities substantial flexibility in setting customer classifications, and will uphold Commission approved classifications so long as the Commission's decision is "fairly debatable."[331] The Company's development of a straight-forward customer classification based solely on the purpose of the use, i.e. resale, is fully authorized by the statute and entirely consistent with other utilities across the Commonwealth.[332]

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[329] Oct. 13, 2026 Hearing VR (5:17:14 PM – 5:18:55 PM).
[330] KRS 278.030(3)(emphasis added).
[331] *Nat'l-Southwire Aluminum Co. v. Big Rivers Elec. Corp.*, 785 S.W.2d 503, 514-515 (Ky. Ct. App. 1990). *See also Public Service Com'n of Ky. v. Commonwealth*, 320 S.W.3d 660, 667 (Ky. 2010).
[332] Reviewing other water utilities' definitions of their resale customer classes confirmed that the Company's classification is standard practice:

> Wholesale; This class applies only to other water systems that have been assigned a Public Water System Identification number and operate as an independent water system purveyor and re-sell water to their own customers. The wholesale rate shall apply in addition to any state required taxes or fees and any other contractual franchise fees. In order to purchase water under the Wholesale Rate, the customer must first sign a Wholesale Customer User Agreement as set forth in this tariff and must pay any Meter Connection Fees, System Development Charges or other improvement costs as required in the User Agreement.

Tariff of Hardin County Water District No. 1, Sheet No. 8 (Effective Apr. 11, 2002).

"Wholesale customer service consists of water sales made for re-sale purposes." Tariff of Hardin County Water District No. 2, Sheet No. 12.1 (Effective June 13, 2025).

"'Wholesale customer' means a customer that is a private or public water utility, including a city, that purchases water for resale to its customers." Tariff of Ohio County Water District, Sheet No. 4 (Effective Oct. 31, 2024).

Additionally, GMWSS has not presented any evidence that the Company's Sales for Resale rate is unlawful. GMWSS's assertion that its legacy contracts with Harrison and Nicholas Counties demonstrate the unreasonableness of the Sales for Resale rate is both analytically and practically flawed. First, the reasonableness of the Harrison and Nicholas County special contracts and the reasonableness of the proposed Sales for Resale rate are *separate inquiries*. Whether the Harrison County and Nicholas County special contracts are reasonable must be evaluated based on the unique circumstances of those contracts and has no bearing on the reasonableness of the Commission's approved Sales for Resale rate.[333] Intermingling the two questions serves GMWSS's purposes, but it has nothing to do with sound ratemaking. Further, the Company's inclusion of these customers in its cost-of-service study has no real impact on the Commission's final analysis. As the Commission has acknowledged, a well-supported cost-of-service study is the starting point of ratemaking, not the sole consideration.[334]

Second, developments since the hearing in this case have rendered GMWSS's argument, effectively, moot. In response to a post-hearing data request, the Company explained that a new contract with Harrison County Water Association has been reached and that the effect of that new contract is to reduce KAWC's proposed Sales for Resale rate to $7.1173 per thousand gallons.[335]

More importantly, despite GMWSS's misgivings about its inclusion in the Sales for Resale class, KAWC has offered to discuss a special contract with GMWSS, subject to Commission approval. At the hearing, Mr. Azevedo acknowledged that KAWC had reached out to discuss a special contract rate with GMWSS in 2025, and that William Lewis had proposed developing a

[333] *See The Application of Louisville Gas & Electric Company to Adjust its Gas Rates and to Increase its Charges for Disconnecting Service, Reconnecting Service and Returned Checks*, Case No. 2000-00080, Order at (Ky. PSC Sep. 27, 2000) (finding that if a special contract covers variable costs and contributes to fixed costs, "the system as a whole and the remaining customers benefit.").
[334] *Proposed Adjustment of the Wholesale Service Rates of Hopkinsville Water Environment Authority*, Case No. 2009-00373, Order at 7 (Ky. PSC July 2, 2010).
[335] KAWC response to PSC PH-11 (Oct. 30, 2026).

direct line of communication in 2026.[336] Mr. Azevedo further agreed that open dialogue would be to the GMWSS's benefit, but that he had deferred to GMWSS's legal representation on the matter.[337]

Finally, any arguments GMWSS seeks to raise GMWSS's meter charges as compared to meter charges to Bulk Sales customers further demonstrate that GMWSS is trying to turn a rate case into a customer dispute. As the Company addressed in post-hearing discovery, meter charges to Bulk Sales customers, like any other customers, are evaluated on a customer-by-customer basis, and do not support special treatment for GMWSS.[338]

GMWSS is an appropriately classified customer taking service at Commission approved rates. It cannot rely on a single special contract to argue that it is paying an unreasonable rate, and it has produced no cost-of-service data to support a different rate for its customer class. The Company remains open to discussions with GMWSS about resolving any service issues or developing a special contract rate, and GMWSS's General Manager generally agrees that these discussions would benefit both parties. In short, GMWSS has not raised any issues that the Commission needs to address or resolve in this proceeding.

**(B) <u>Single Tariff Pricing</u>**

During the hearing, LFUCG attorneys raised concerns about existing customers subsidizing customers in KAWC's newly acquired systems, and asked if KAWC expected its existing customers to make up the difference if these newly acquired systems are more costly than expected.[339] The Company has demonstrated in the record of this case that concerns about cost-

[336] Oct. 14, 2026 Hearing VR (11:28:00 AM – 11:33:51 AM; 11:37:54 AM – 11:40:10 AM).
[337] Oct. 14, 2026 Hearing VR (11:30:47 AM – 11:33:51 AM).
[338] KAWC response to GMWSS PH-4(a).
[339] Oct. 13, 2026 Hearing VR (3:54:20 PM – 3:56:10 PM). In a similar vein, GMWSS questioned the reasonableness of requiring transmission customers to cover costs from the Company's distribution customers and asked whether KAWC's Sales-for-Resale rate was a tool to promote regionalization. Oct. 13, 2026 Hearing VR (2:16:55PM – 2:17:23 PM); KAWC response to GMWSS 1-6.

subsidization are unfounded, and that single tariff pricing facilitates regionalization and benefits customers by spreading costs across a larger customer base.

The Commission has supported KAWC's commitment to single tariff pricing for more than 20 years. In its order approving the Company's acquisition of the Owenton system in 2005, the Commission ordered the Company to propose a single tariff pricing structure in its next rate case.[340] The Company first proposed single tariff pricing in its 2007 rate case, and the Commission ultimately approved a single tariff proposal included in a joint stipulation of parties to the case, including LFUCG.[341] When the Company proposed the Northern District Connection project and sought cost recovery from its entire customer base, though, LFUCG reversed course, arguing that LFUCG and other Central Division customers should not pay for a project that would not benefit them.[342]

Although the Commission's order in the CPCN proceeding acknowledged that single tariff pricing was "not without its costs," the Commission expressed its continued support for regionalization and single tariff pricing in its subsequent rate case order:

> Based on our review of the record, we find that Kentucky-American's unified rate structure should remain in place. The Commission has consistently supported the concept of a unified rate structure to encourage consolidation of water systems and to improve the quality of water service in the Commonwealth. Reversal of this policy would discourage further water system consolidation.[343]

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[340] *Joint Application of the City of Owenton and Kentucky-American Water Company for Approval of the Transfer of the Ownership of the Assets of the City of Owenton to Kentucky-American Water Company*, Case No. 2005-00206, Order at 6 (Ky. PSC July 25, 2005).
[341] *Adjustment of Rates of Kentucky-American Water Company*, Case No. 2007-00143, Order at 3 (Ky. PSC Nov. 29, 2007).
[342] *Application of Kentucky-American Water Company for a Certificate of Public Convenience and Necessity Authorizing Construction of the Northern Division Connection*, Case No. 2012-00096, Order at 18-19 (Ky. PSC Feb. 28, 2013).
[343] *Application of Kentucky-American Water Company for an Adjustment of Rates Supported by a Fully Forecasted Test Year*, Case No. 2012-00520, Order at 70 (Ky. PSC Oct. 25, 2013).

Intervenors again questioned the reasonableness of single tariff pricing during the Company's 2018 rate case, which centered around the Company's acquisition of the Eastern Rockcastle Water Association and North Middletown's municipal water system.[344] Citing its 2007 and 2012 rate case orders, the Commission reaffirmed its support for KAWC's unified tariff, finding that approval was consistent with its precedent and supported by the evidence.[345] As recently as February, the Commission recognized that "it is the public policy of the Kentucky is to encourage regionalization, consolidation, and merger of water utilities."[346]

As in these prior cases, the evidence in this proceeding fully supports the demonstrated benefits of single tariff pricing and regionalization. As discussed above, the acquisition of the Livingston, WSC, and Black Mountain systems will help the Company maintain O&M cost control across its customer base, finding that the acquisitions will reduce its annual O&M costs by $29.14 per customer.[347] At the hearing, Mr. Burton explained the fundamentals of how single tariff pricing improves outcomes for existing customers:

> So the reality of those existing customers, of our existing customers, what I would say to them is if we were to stay 100% static and never have a growth in customers either organically or through acquisitions, the cost of providing them services will increase over time due to the replacements needed in the assets that provide the service to them [and the] inflationary pressures on costs of providing those services. But a larger customer base allows those costs to be moderated and spread out across a larger footprint, which is the basis of single tariff pricing and why it works and literally why regionalization and economy of scale work.[348]

In short, the Commission has consistently recognized the system-wide benefits of the Company's single tariff pricing, finding that the Company's rates promote regionalization and its

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[344] *Electronic Application of Kentucky-American Water Company for an Adjustment of Rates*, Case No. 2018-00358, Order at 70-72 (Ky. PSC June 27, 2019).
[345] *Id.* at 70.
[346] *Application of the City of Livingston and Kentucky-American Water Company for the Transfer of Control and Assets*, Case No. 2025-00364, Order at 15 (Ky. PSC Feb. 10, 2026). *See also* KAWC response to GMWSS 1-4.
[347] Prendergast Rebuttal at 21.
[348] Oct. 13, 2026 Hearing VR (10:01:30 AM – 10:02:38 AM).

accompanying benefits. Based on the evidence in this case, the Commission should recognize that supporting the Company's continued use of single tariff pricing remains the right decision.

**(C) Prudent Capital Expenditures**

Throughout the case, Intervenors have questioned the necessity of the Company's planned capital investments and suggested that the investments are driven by shareholder returns rather than operational need. At the hearing, for example, LFUCG Mayor Linda Gorton criticized the Company's rate increases, suggested both that the Company's investments in the LFUCG portion of its system were unreasonable and that the SIP would accelerate the pace of investment in its system.[349] Her comments seem to suggest that the Company plans to increase its capital investments without a system need or basis to do so. This is simply not the case. KAWC's infrastructure investments are driven by the Company's need to deliver adequate and reliable service and are developed independently of cost-recovery or earnings-related considerations. Commissioner Wood allowed KAWC President Robert Burton an opportunity to address this issue directly:

> **Wood**: Mr. Burton, thank you for taking the stand. Again, I'll try to be brief. I've got some concerns that Kentucky-American is intentionally increasing their capital expenditures in order to increase profits. And I have seen material, American Water material that basically says in 2021 that they went from a seven to eight percent goal of increases in expenditures to eight, eight to nine percent. And I understand that you were not employed at that time and you may not know about any of that information, but I want to know do you receive direction from American Water in terms of how much capital expenditures to spend every year?
>
> **Burton**: Frankly, sir, no. We do not receive direction on what to spend. We don't receive direction on what to artificially either spending capital or to artificially change in a rate base standpoint. I believe some of the documents you are referring to are likely information we give to investors, information we give to the SEC, and our quarterly and annual filings.
>
> The reality is, what [ends] up discussed in those situations as targets and metrics are absolutely built from the ground up on reality and what is actually

[349] Oct. 13, 2026 Hearing VR (9:15:40 AM – 9:17:57 AM).

occurring or forecasted to occur, which then, in the language of investors, becomes a target of the future or things that are going to occur. So, it doesn't start with a target and then work our way back to what does it takes to achieve the target. It starts with reality.

When it comes to capital planning and capital spending, as was testified in testimony by Mr. Magner, there was extremely extensive amount of analysis work that goes into what is needed to spend on infrastructure and infrastructure needs to have replacement, timing of that replacement. Truthfully the gating factor to what is put into investment is really two things. It's the ability to attract the capital, either through debt or equity to fund those investments, or the reality of trying to maintain affordability to customers. As was testified by Mr. Rea in his direct testimony and supplemental, is the fact that, rates in Kentucky-American Water are absolutely not only within the range of affordable metrics, which are put out by the EPA to Congress on expectations on a percentage of cost against medium household income (percentage of income corrected to percentage of cost during testimony). We're well within those, maintaining well within those, and projected to be well within those. That is a gating factor to us.

The reality of the needs of capital programs and capital spending, as Mr. Magner testified, goal would be to get, based on our analysis, closer to, on pipeline for instance, 0.8 to 1.2 percent replacement rate, which we are not currently at. But we are hoping to get closer to that so that we can again maintain reliability of the system and maintain service to customers. We could arbitrarily make the decision in a case such as this to double our capital plan for next year. Instead of $108 million we could have put $200 million into it and could absolutely justify the need for the capital spending. But it would not be a balance of affordability and what is right for our customers of both doing the investment that needs to be done, making the replacements as they need to be made, but balancing the fact that at the end of the day someone has to pay for that. So we're trying to always balance those factors.

The buildup of all those costs do a few things. They become capital spending that needs recovery. They become capital spending that needs debt and equity to fund those. And those work their way into other parts of the business such as rate base. And if you spend more on capital than is needed for those investments, rate base will grow some over time. There is always the other side of that. As items retire or are retired, they come off of rate base, so it's not a one for one. But knowing those things occur, they become metrics that we understand as a company that we need to report to our investors, we need to tell to the market, because we are a publicly traded company. So those numbers that are built up on actually what is going on and actually what is needed become information that we supply, and in the language of those conversations it becomes quote, unquote targets because we're targeting where this is where it's going to go based on the actuality of what is occurring.

> So we don't start with the target and work our way backwards, we start with reality and it works its way up to what becomes spoken of as a target.[350]

KAWC's approach to planning its capital investments, along with other operating efficiencies discussed throughout this case, have generated measurable benefits for its customers. As the Company explained in post-hearing discovery, KAWC has kept cost increases below the CPI inflation rate for water and sewer maintenance, and, based on data since 2014, KAWC's average residential customer bill is $2.41 *lower* than it would have been at the water and sewer maintenance CPI rate.[351]

LFUCG's own experience with deferred maintenance illustrates the risks of delaying necessary system investments. In 2006, the United States Environmental Protection Agency ("EPA") filed suit against LFUCG for violations of the Federal Clean Water Act.[352] According to case records, the sources of the violations were numerous locations across LFUCG's sanitary sewer system that were regularly overflowing and releasing unpermitted discharges into Waters of the United States.[353] As LFUCG states on its own website:

> Over the years, Lexington had failed to properly maintain both the sanitary and storm sewer systems. Age, changing regulations and equipment failures related to deferred maintenance created an assortment of operational problems, but the end result of those problems has been that during significant rainfall, we have been discharging sewage into our streams in violation of the Clean Water Act.[354]

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[350] Oct. 14, 2026 Hearing VR (10:20:30 AM – 10:25:28 AM) (lightly edited for clarity)
[351] KAWC response to PSC PH-16.
[352] *United States, et al. v. Lexington-Fayette Urban Cnty. Gov.*, Case No. 5:06-cv-00386-KSF, Compl. (E.D. Ky, Nov. 20, 2006).
[353] *United States, et al. v. Lexington Fayette Urban Cnty. Gov.*, Case No. 5:06-cv-00386-KSF, Consent Decree at 2 (E.D. Ky. Jan. 3, 2011) ("Consent Decree"). A link to the Consent Decree is on LFUCG's website at the link in FN 354 below.
[354] *U.S. EPA Consent Decree*, LFUCG, https://www.lexingtonky.gov/government/departments-programs/environmental-quality-public-works/water-quality/us-epa-consent-decree (Last accessed Nov. 9, 2026).

On January 3, 2011, the parties entered a Consent Decree into the record of the case, which required LFUCG to pay a civil penalty of $425,000 and undertake significant infrastructure repairs.[355]

LFUCG's experience illustrates the consequences of deferring necessary infrastructure investment. Following the Clean Water Act enforcement action, LFUCG was required to undertake extensive improvements to its sewer system. LFUCG's website acknowledges that deferred maintenance contributed to the conditions giving rise to those required repairs, and LFUCG has since established the Water Quality Management Fee to provide a funding source for stormwater projects required by the Consent Decree[356] and annual increases to its sewer rates.[357] This experience underscores the point Mr. Burton made at the hearing, which is that necessary infrastructure investment cannot be avoided indefinitely. Deferring capital investment may postpone costs in the short term, but it does not eliminate the underlying system need and may ultimately require substantial corrective action. KAWC's capital planning seeks to address infrastructure needs on a proactive, planned basis while balancing those needs against customer affordability. That approach should not be construed as investment undertaken simply to increase rate base or shareholder returns.

## VIII. CONCLUSION

KAWC supported the entirety of its request for rate relief through record evidence in this proceeding. The Company has met its burden of proof with respect to demonstrating the

[355] Consent Decree at 14.
[356] Lexington-Fayette Urban County, Ky., Ordinance No. 73-2009 (May 14, 2009); Lexington-Fayette Urban County, Ky. Code of Ordinances Art. XIV, § 16-401 *et seq.* (2009); LFUCG Council Meeting Minutes May 14, 2009). *See also* KAWC Post Hearing Data Request No. 3 to LFUCG, Attachment at 20-43 (Oct. 22, 2026).
[357] Lexington-Fayette Urban County, Ky., Code of Ordinances §§ 16-48, 16-57.1, 16-59, 16-59.1, 16-60; Lexington-Fayette Urban County, Ky., Ordinance Nos. 34-2008 (Feb. 21, 2008); 84-2008 (Apr. 24, 2008); 85-2012 (July 5, 2012); 22-2015 (Mar. 17, 2015); 34-2019, § 34-2019 (June 6, 2019). LFUCG Council Meeting Minutes Feb. 21, 2008). *See also* KAWC Post Hearing Data Request No. 3 to LFUCG, Attachment at 1-19.

reasonableness of its proposed revenue requirement, including employee-related costs, working capital allowance, miscellaneous expenses, rate case expenses, and unaccounted-for water loss. The Company's proposed SIP and related capital investment plan are well calibrated to increase the interval between rate cases; maintain and improve the Company's system; and encourage prudency and transparency. The capital structure and ROE that KAWC has requested are reasonable and premised on the prudent application of a host of cost of equity estimation models. The Company would be placed at a competitive disadvantage if Mr. Rothschild's recommended ROE is adopted.

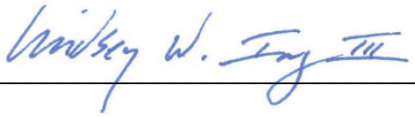
KAWC respectfully requests that the Commission approve revisions to the Company's tariff and the requested increase in rates to ensure that the Company is afforded the fair, just, and reasonable rates to which it is entitled.

Respectfully submitted,

Lindsey W. Ingram III
L.Ingram@skofirm.com

Monica H. Braun
Monica.Braun@skofirm.com

STOLL KEENON OGDEN PLLC
300 West Vine Street, Suite 2100
Lexington, Kentucky 40507-1801
Telephone: (859) 231-3000
Fax: (859) 259-3503

BY: 

Attorneys for Kentucky-American Water Company

## CERTIFICATE

In accordance with the Commission's Order of July 22, 2021 in Case No. 2020-00085 (Electronic Emergency Docket Related to the Novel Coronavirus COVID-19), this is to certify that the electronic filing has been transmitted to the Commission on November 9, 2026; and that there are currently no parties in this proceeding that the Commission has excused from participation by electronic means.

STOLL KEENON OGDEN PLLC

BY: _____

Attorneys for Kentucky-American Water Company